UNITED STATES
FEDERAL COMMUNICATIONS COMMISSION

IN RE:)
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WCB WORKSHOP)

Pages: 1 through 193

Place: Washington, D.C.

Date: April 6, 2011

HERITAGE REPORTING CORPORATION
Official Reporters
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

IN RE:)
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WCB WORKSHOP)

Room TWC 305
FCC Building
445 12th Street, S.W.
Washington, D.C. 20554

Wednesday,
April 6, 2011

The parties met, pursuant to the notice of the Commission, at 9:15 a.m.

ATTENDEES:

ALBERT LEWIS, CHIEF, PRICING POLICY DIVISION, WCB
KRISTA TANNER, BOARD MEMBER, IOWA UTILITIES BOARD
MELISSA NEWMAN, VICE PRESIDENT, FEDERAL REGULATORY AFFAIRS, CENTURYLINK
DAVID ERICKSON, FOUNDER/CEO, FREECONFERENCECALL.COM
DAVID FRANKEL, FOUNDER, ZIPDX
MICHAEL ROMANO, SENIOR VICE PRESIDENT OF POLICY, NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION (NTCA)
JONATHAN BANKS, SENIOR VICE PRESIDENT, LAW AND POLICY, USTELECOM
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MICHAEL J. COPPS, COMMISSIONER, FCC
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ATTENDEES: (CONT')

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P R O C E E D I N G S

(9:15 a.m.)

CHAIRMAN GENACHOWSKI: This is the first workshop in the Universal Service Intercarrier Compensation Reform proceeding. Welcome to those in the room, those joining online, where the workshop, like all of our workshops, is being livestreamed. We have a great panel lined up today. I'd like to thank a number of people knowing that I won't be able to thank everyone, but a special thanks to Krista Tanner from the Iowa Utilities Board, Peter McGowan, the general counsel for the New York State Department of Public Service, and to all of our panelists for taking the time to be with us here today.

I know many of you have travelled a great distance to be here, you're probably feeling lucky that you didn't have to travel yesterday, which would not have been that much fun. But I appreciate your commitment to being here with us in this room where a lot of sleeves will be rolled up today, looking to get some work done. Let me again thank the staff of the FCC, both those who organized this particular event and the team that's been working on USF and ICC reform for some time now and making just wonderful progress.

Why are we here? We're here for a simple reason. The Intercarrier Compensation system is broken, and fixing it is vital to achieving our country's broadband goals. The ICC system was created decades ago for a telephone network that no longer exists.

In the face of dramatic changes in market and technology, the current ICC system is actually impeding the transition to all IP networks and distorting investment incentives. There's no defense of a tangled ICC system acting as an obstacle to bringing the benefits of broadband to all Americans. That's why reform designed to remove impediments and modernize the system is critical now.

Now ICC reform is a top priority for all of us on the Commission. Not easy. It's been tried several times over the last decade. But when this Commission voted unanimously to move forward with reform earlier this year and again in an unprecedented unanimous blog post by all five Commissioners a few weeks ago we made clear that we are all committed to reform and to moving to order soon within a few months of the completion of the record in May.

With that timing in mind, today is the day to discuss the path forward on intercarrier compensation reform. I look forward to a healthy discussion from our panelists and other participants, and I expect stakeholders to work together to find common ground, not to rest on old talking points.

A couple more points. First I appreciate the efforts many states have taken to reform state access charges. I'm particularly pleased that Tennessee and Washington State have recently taken steps to reduce access charges. These states join more than a dozen others, including Nebraska, Kansas, Michigan, Iowa, Texas, Georgia, that are leaders on ICC reform. I call on other states to follow these states' lead and take on the challenge of intrastate access reform. Such efforts are an essential part of the reform process, and we can learn from them as we work together to do the rest of the work necessary to achieve comprehensive reform.

Second, good policymaking requires good data, and nowhere is that more true than intercarrier compensation reform. I'm committed, as we all are, to data-driven policymaking, and this reform process is no exception. I encourage everyone affected by ICC reform, both ICC payors and payees, to file the ICC data requested in our notice of proposed rulemaking. Some stakeholders have already filed the requested data, and I thank you for doing so. Others have not.

Now we will move forward with reform using the best data we have. Stakeholders that don't provide data face real risks. Without your data, without the data we need to evaluate your positions, including claims of need for universal service support, those positions have little chance of shaping our ultimate reforms.

So again, thank you to all of you for participating in this important workshop. I want to thank all of my colleagues who have agreed to participate. I see Commissioner Copps. I saw him. Commissioner Clyburn, Commissioner Baker, Commissioner McDowell.

Before I turn the floor over to my colleague, Commissioner Copps, I want you all to know that Commissioner Copps, when we were talking about USF and ICC reform I guess a couple of months ago as we were preparing to move forward on the notice, said we should think very seriously about organizing stakeholders together in a process of workshops where people will work up their sleeves and get things done, and it was exactly the kind of thing that the staff and I had been thinking about. All of the Commissioners agree on this. Commissioner Copps, I want to thank you for pushing us as you always do, and with that, let me hand the floor over to Commissioner Michael Copps.

COMMISSIONER COPPS: Thank you very much. Is this on? I can talk from here? Thank you, Mr. Chairman. Thank you for your leadership in getting us all here today and for teeing this up for action if we can get this done, and I think we will. It's going to be a historic achievement of considerable magnitude.

I am delighted to be here this morning. I'm even more delighted to see all of you good folks here. This is an important meeting that can set us on the road to a viable system of intercarrier compensation and universal service reform, so I'm just happy to be a part of it.

I think the blog posting that the Chairman mentioned kind of said it all and indicated to everybody that the Commission is dead-serious about getting this done this year, getting it done long before the end of this year. To do that, it's going to take a lot of work, it's going to take a lot of sacrifice on all of our parts, but we begin today with our work toward a viable system. We're not here to discuss Christmas wish lists or things like that. I think we're here all cognizant of the fact that we are approaching an end game on this and this is a time to really get down to the remaining differences that are still out there and calling for attention.

We all know the intercarrier compensation system is byzantine, it's broken, as the Chairman said. Yet we all know that it's been around for a long period of time and it's part of the system and has a long history, and as we move ahead we have to be cognizant of that history and sensitive to the needs to a transition plan that will move us sensibly and rationally with minimum dislocation toward a more viable system in the future.

I also want to agree with what the Chairman said about the important role that the states should be playing and will be playing and already are playing as we move these important items forward. We've got to come up with a system that's got some credibility. What we have now has no credibility here, no credibility on Capitol Hill, no credibility in the financial markets, no credibility with the American people, so we've got some considerable work to do.

And with that, I'll turn the microphone over to others, but again thank you all very much for coming. Commissioner McDowell is here. Commissioner, I guess would you like to say a few words?

COMMISSIONER MCDOWELL: Just to keep you all guessing, I'll do it from up here. How's that sound? Good morning. Thank you all for coming. You have a very full, long day ahead of you. I hope that if you find that you have differences of opinion that you continue to work through them.

As I was listening to my friend and colleague, Mike Copps, speaking, I was reminded of the fall of 2008, which on the one hand doesn't seem like that long ago, on the other hand it seems like a decade ago. But we're four Commissioners, two Republicans, two Democrats, of which he and I were a part. We came to agreement on many of the thornier issues on intercarrier comp and universal service reform. It unfortunately just didn't happen, so here we are today. And we need to go forward. I want us to go forward as quickly as possible.

Of course I've been saying for some time now that I think we should be tackling distribution and contribution and intercarrier compensation all at the same time. I've said many times, it's become a cliché at this point, it's sort of like fixing a watch. It's hard to tinker with one component of it without affecting all of the other components. But if we're going to start off with the distribution side, I'm all for that. Let's get it tackled.

You know, as I see the trees budding here in Washington, this is one of my favorite times of year except for the allergies it gives me, but anyway, that's another story. But it's absolutely a beautiful time of year as we see that newness, that new green coming out of the trees, maybe we could all make a pledge today that we can have agreement on comprehensive universal service and intercarrier compensation reform before those leaves fall of those trees this year. So I hope you'll all pledge with me to do just that.

But the system is bloated. It is antiquated. It is inefficient. It is broken. And the inability of government to resolve this issue is part of what makes people cynical about the ability of government to solve basic problems. This is one of the fundamental duties of the Federal Communications Commission is to solve the universal service and intercarrier compensation problem. Congress tried this the last time I remember 15 years ago through Section 254.

It's important to listen to all stakeholders, but there's no particular constituency we should be worried about other than the American consumer because at the end of the day it's American consumers who contribute to a subsidy that then others receive in theory to help subsidize other consumers. But we need to go forward and do this quickly because, if not, then we're not doing our basic jobs as public servants, and that would be shameful if we can't come to agreement.

So I don't think we also should wait for Congress. I respect the advice from Congress, but if the House and the Senate want to agree on legislation and the President wants to sign it, I will dutifully implement it. But we have spent 15 years waiting for Congress to revise universal service and it hasn't happened, so we should go forward. It is our duty. It is what Congress has told us to do through the plain language of the statute, and we should go forward and do that as quickly as possible.

So, in a way, I feel as if we should close the doors and lock them and not let anyone leave until this problem is solved today. Realistically I know that's not going to happen, but I do hope it will happen before the leaves fall of the trees. So, without further ado, we're here to help and to listen. We have a lot going on this week. We have an open meeting tomorrow with some other hot potato issues on the agenda as well, so I've got to go work on those, but I look forward to working with all of you, but let's hurry up and get our work done. Thank you very much.

Well, I should introduce my colleague then. Let's see. Next, Commissioner Clyburn, the chair, Chair Clyburn of the Joint Board, I'm sure has many things to say on this topic. Thank you.

COMMISSIONER CLYBURN: Thank you, sir. You've said most of them, but thank you. I appreciate it. Good morning, everyone. I'd like to join in the chorus in thanking the panelists for participating in today's workshop. I also would like to acknowledge the FCC staff for their diligence in planning this workshop. I know a great deal of advance planning must be done for these workshops to be successful, and I want to formally thank all of you who played a role.

I would not feel comfortable this morning if I did not also thank Commissioner Copps. He recommended that the agency conduct workshops on universal service and intercarrier compensation reform to encourage dialogue and consensus-building, and again I would like to thank you for that. I wholeheartedly agree with him. I agree with him a lot of the time. But I wholeheartedly agree with him that these workshops have that potential in terms of consensus-building, and it is my hope that today's inaugural workshop on this issues will do just that. These issues are of vital importance to ensuring that every American has access to both affordable voice and broadband service no matter where they live, and I look forward to the exchange today in order to get there. Thank you so very much.

COMMISSIONER BAKER: Last but not least or maybe least, I don't know. The benefit of going last is that I do get to be brief, so I want to commend and associate myself with all the words of my esteemed colleagues and Chairman. I think having all five Commissioners at a workshop, if it's not completely unprecedented, it's pretty close. It's definitely rare, and I think that fact alone is telling for how important this is.

So again I won't repeat what you all have said, but I think we all hope that we have a chance here for real reform and we're all extremely grateful that you're here. Reform needs to happen sooner rather than later. I really think that to me universal service, ICC reform and spectrum reform are agenda items 1 and 1A on our to-do list for 2011, and I appreciate my colleagues' commitment to both of these things.

The approach that we take today I think to just say address these things head on and a number of the most vexing issues that have been before us is the right one. We have left a lot of these questions, such as phantom traffic, access stimulation and VoIP compensation, we've just left them to linger for way too long, and so I really appreciate the agenda today. I welcome our focus on these things first, and I'll be particularly interested to hear the perspectives about how the IP-based services should be incorporated into a circuit-switched world in an efficient and equitable manner.

And not to be left out of this afternoon's panels, we're going to focus on an issue that has not received sufficient focus, what type of recovery reform revenue recovery mechanism is needed to offset the lost intercarrier compensation payments and how to square any of the new mechanisms with the need to control the size of the fund. There are so many issues to negotiate, but the fund size should not be one. We cannot afford to let the fund continue to grow unchecked.

I again want to add my thanks to the Wireline Bureau for pulling together this event, and I really thank today's panelists. Having such an esteemed crowed here is really helpful. I thank you for participating and hopefully working with all of us hand in hand as we work to find the compromises that are going to be necessary to place our universal service and intercarrier compensation regimes on firmer footing in an IP world. So good luck today. We are anxious to hear your thoughts, your expertise, and thanks again for being here.

MR. LEWIS: Good morning. I'm Al Lewis in the Pricing Policy Division of the Wireline Competition Bureau. Welcome and thank you to our panelists for the first workshop through which the Commission will hear the perspectives on interested parties on the issues presented in the universal service and intercarrier compensation notice of proposed rulemaking.

We are eager to hear and learn from the perspectives of consumer representatives, state authorities, industry analysts and industry participants. In our first of three sessions today, we will focus on arbitrage activities that are occurring in the market as a result of the current intercarrier compensation system. In particular, our panelists have been invited to comment on proposals to address phantom traffic, the delivery of calls with insufficient information to identify who delivered the call or where it came from, and access stimulation, arrangements between local exchange carriers and providers of high-volume services designed to radically increase the number of incoming calls and intercarrier compensation revenues.

Our first session is scheduled for an hour and 15 minutes, so I will quickly introduce our panelists. Each panelist will then summarize their positions or proposals in three minutes or less and we will turn to questions from the audience in person and online and our expert questioners to engage our panel in what I'm sure will be a lively discussion. If members of the audience would like to submit questions for the panel, we have notecards available from our staff, so just write your questions on the cards and the staff will bring them up to the panel. For our online audience members, you can email questions to iccreform@fcc.gov.

Our panelists this morning, from left to right, Iowa Utilities Board Member Krista Tanner; Melissa Newman, Vice President, Federal Regulatory Affairs, CenturyLink; David Erickson, founder of FreeConferenceCall.com; David Frankel, the founder of ZipDX; Michael Romano, Senior Vice President of

Policy, National Telecommunications Cooperative Association; Jonathan Banks, Senior Vice President, Law and Policy, U.S. Telecom; and Dave Schornack, Director of Business Development for TekStar Communication. Thank you. And, Krista, if you'd like to get us started.

MS. TANNER: Okay. Well, thank you and first of all I'd like to thank the FCC for inviting me to participate today and not only for my invitation today, but it has not gone unnoticed among the states how inclusive this FCC Commission has been and has invited the states to participate in these dialogues every step of the way, and that is very much appreciated.

As the notice of proposed rulemaking noted, the Iowa Utilities Board has taken steps to address traffic pumping in Iowa. Last year the IUB issued rules governing the intrastate access charges that may be assessed by carriers engaging in what the IUB has termed high-volume access services. The IUB announced its intent to create these rules at the conclusion of a contested case that involved a formal complained filed by Qwest against eight Iowa LECs who were engaged in traffic pumping activities via agreements with conference calling companies. The board ultimately found that the traffic associated with the conference calling companies was not subject to the LECs with access tariffs. The conclusion was based upon the findings that the companies were not end users under the tariffs, assuming they were end users. The traffic was not delivered to an end user premises, as required by the LECs tariffs. And in the case of six of the respondent LECs, the traffic did not even terminate in a LECs exchange, as is necessary for a LECs tariff to apply.

Based on these findings, the IUB ordered that the charges were inappropriate and ordered refunds of the access charges, but because the IUB's findings were based largely on tariff violations, the IUB was concerned that in the future LUCs could enter into revenue sharing agreements with free conference calling companies in a way that conformed to their tariffs and then would continue on with these arbitrage activities. So to curb these future arbitrage abuses, the IUB initiated a rulemaking to address the intrastate access rates associated with high-volume traffic in those areas where access rates have been set high to reflow low-traffic volumes.

The approach that we took in our rules was based on the argument made by the LECs that Qwest's complaint was really about rates, that is, how much the IXC has to pay for terminating toll traffic as the volumes of that traffic increase, so based on these arguments the board initiated the high-volume access rules on which the FCC has sought comment as an alternative to its proposed rules.

So I have just given you a very brief overview of how those rules came to be, and I would be happy throughout this workshop to answer more detailed questions regarding those rules. And with that, I'll end my comments, and again thank you for inviting me.

MS. NEWMAN: Is this on? I am pleased to be here today, and I applaud the FCC for teeing up phantom traffic and access stimulation issues in the NPRM and for adopting an expedited comment cycle. I'm also pleased to announce that this is my first public appearance since CenturyLink and Qwest merged last Friday, hence the green scarf. The combined company, CenturyLink, operates in 37 states. CenturyLink is the third largest phone company in the country and notably 74 percent of CenturyLink's service territory is in low-density, high-cost areas with fewer than 30 people per square mile.

The common theme for this panel is gaming, taking advantage of the rules or lack thereof to manipulate the system to make windfall profits. I'll first talk about phantom traffic. The NPRM rightly describes phantom traffic as improper arbitrage. Carriers disguise the nature or source of the traffic in order to avoid or reduce their access payments. Phantom traffic is not inadvertent loss of identifying information. It's deliberate cheating by a carrier intentionally evading compliance with the FCC's intercarrier compensation rules. It undermines the foundation of universal service and it distorts competition.

The NPRM's proposed rules are a great starting point. They would prohibit altering, stripping or omitting calling number information. CenturyLink has long supported U.S. Telecom's interim proposal. It is straightforward. Originating carriers must transmit identifying information and intermediate carriers must pass that information on. CenturyLink believes the FCC should go even further and state that the principals of the T-Mobile decision should apply so that ILECs can invoke the negotiation processes if other carriers refuse to enter into agreements with us.

Turning to traffic pumping, it is an unlawful scheme to arbitrage switched access rates that were designed for rural low-volume areas. It results in carriers being billed tens of millions of dollars, all to provide windfall profits to high-volume free conference call and chat services with their lax ILEC partners. CenturyLink has for a long time urged the FCC to end this abuse. The NPRM proposes to do so using a hybrid approach, and we applaud that approach. CenturyLink has some additional measures we would take, but the approach in the NPRM is a great starting point.

In addition, we also think the FCC should confirm that tariffs filed or maintained to start or continue this unlawful practice violate the Communications Act and should not get Section 204 protection. A tariff that was deliberately unlawful when filed can't be then deemed lawful.

We really appreciate the FCC inviting CenturyLink to be on this panel. We're very interesting in working with the industry and the FCC to stop these practices. Thank you.

MR. ERICKSON: I'm David Erickson with Free Conferencing Corporation. I really appreciate being here, and I thank all of you for coming.

What we do is we do toll conferencing. Historically terminating access has been paid on toll conferencing. What we did different is we took the organizer fees out of toll conferencing. Our average user uses 28 minutes per month per year. That's all the minutes they use. It's not an abusive practice in the form of minutes. The average call size is five people. Toll conferencing in its nature, right, reduces the amount of long distance that a person uses. If you don't believe me, cancel your next conference call and try doing it person to person and see how much long distance you use.

We operate in the Americas, in Africa, in Europe, in Asia and in Australia with the same business model. Domestically we are in both rural and urban areas. We have nine locations in rural areas, seven in urban areas. Of the nine in rural areas, four operate with a high-volume access tariff that reduces the tariff as volume goes up. All of the nine have direct relationships or direct connections to the wholesale marketplace.

Some of the companies opposed to what we do are engaged in price wars in the wholesale marketplace, meaning if we unload the traffic, they try and take it back by lowering their price. I feel that toll conferencing is not the problem. Presidential campaigns use it, Congress uses it, the

Senate uses it. Revenue sharing is not the problem, but I feel that pricing is the problem, and I want to work towards a pricing solution for our pricing problem.

I like the idea of the revenue sharing trigger. I don't like the idea of a revenue sharing ban. I think that if a revenue sharing trigger triggers something like a high-volume access tariff, it will do two things. One, it will protect the rural LECs that revenue share but don't stimulate access, and the ones that do stimulate access, it will reduce their tariff to a level playing field with the urban areas. By doing that way, you'll incentivize investment in the rural areas, create infrastructure and create jobs in the areas where we need it the most.

I believe that we can arrive at a pricing solution that we could have a deemed lawful status, and I feel it's necessary to have that kind of certainty and that kind of predictability for investment in those areas as well as in urban areas. I completely support this effort and look forward to working with all of you to find a solution.

MR. FRANKEL: Good morning. My name is David Frankel. My business is ZipDX, LLC. We are a conferencing provider. We today do not operate in a mode that uses ICC to our advantage. We pay interstate compensation charges as part of our wholesale arrangements with our underlying service providers.

I've been involved in these proceedings for several years. There are many that I've met who've come before me and I'm delighted that the FCC is now committed to taking action to resolve this.

As we've heard many times, the ICC as an element of supporting and subsidizing rural subscribers is broken and there's a commitment now to fixing it. This particular endeavor is about some interim adjustments while we undertake longer term overall reform. And I'm delighted to see that this is happening. If I thought I could come here today and ask you to codify a regime that would help my conferencing business and give me particular benefits, I would ask you for that.

But what I've seen in the proceedings to date and in your previous actions and in the national broadband plan is that you're not going to do that. You've already decided that that's not the role that ICC plays, even though there are certain benefits that we could probably bring. I'm a clever engineer. I can come up with things we can do. You said you're not going to do that.

So the question now is what are you going to do to help ICC hang on and do what it is supposed to do while you reform the overall program. And certainly, phantom traffic and access stimulations are big pieces that today are being exploited and diverting ICC from that primary mission. So I think that what's been proposed is absolutely necessary. It needs to be undertaken quickly.

I think that when I look under the covers as an engineer at what's going on and what I see is what I call "most-cross routing." As an engineer I just think this is ridiculous. But what you see is you see people locating in locations that are particularly expensive with respect to ICC where they're going to drive a lot of traffic. If you're an engineer, of course you'd go to a lowest cost location if you were going to drive a lot of traffic. That would be the most efficient. You would not insert extra elements into your call path just so that you could collect additional compensation. That doesn't make any engineering sense. It doesn't serve the public good.

So I think as part of this interim action the FCC should not only do what's already been explicitly proposed, but consider some further steps to explicitly say we're not going to permit this kind of gaming. It's not appropriate. The patient is dying here and while we try to let live long enough to let us transition to something more reasonable let's not completely crush it with these additional endeavors.

MR. ROMANO: My name is Mike Romano. I'm the Senior Vice President of Policy for the National Telecommunications Cooperative Association. I just wanted to say thank you to the Commissioners and their legal advisors and the Bureau of Staff for allowing us to participate today.

Turning first to phantom traffic, the question of phantom traffic the practice it complicates or completely obviates the answers to three fundamental questions: Which provider is responsible for the call, what payment is due for the call, and what happens if someone doesn't comply with the rules?

Agreeing with CenturyLink, the notice of proposed rulemaking proposals represent a great starting point for addressing phantom traffic, but I think they only address that middle question, that second question, which is what payment is due for the call. Passing the CPN or charge number without stripping alteration is great, making sure that gets across the indirect networks and platforms a very good start as well. But to answer all three questions, you've got to make sure that more information gets in and stays in the signaling information and/or the billing records that follow.

In particular, to answer the first question about which provider is responsible for the call, you need to be able to tell whom to bill. And CPN or CN don't necessarily answer that question. You're going to need to therefore get the carrier identification code or the CIC or the OCN, the operating company number, which appears in the billing records. And probably also the jurisdictional information parameter, the JIP, the LRN that can appear on the signaling or in the billing records.

Those are the tools that are really needed to answer that first question. And frankly, you know, as people say sometimes, well, phantom traffic doesn't become an issue if unified rates are put into place. That's not true either. You could still have someone not tell you who's sending the call to you. And so having the CIC and the OCN and the JIP and LRN are really important, even in an unified rate environment to identify who is responsible for the call in question. So the rules really do need to go beyond the starting point in the NPRM and address these additional requirements.

You also need to address a few other pieces of this relating to the substitution of CPN or charge numbers, how to identify the jurisdiction of a call based upon the CPN or the charge number. And then also the violation of the rules. What happens? It's hard to say to someone you need to go back and file a formal complaint against this. You need to have some deterrent built into the affect behavior.

On access stimulation, NTCA came out this winter and supported the US Telecom proposal that was filed with a number of other carriers. I think DX was on that as well. And we supported that, by and large. I'd say the most significant question or concern we had was the impact of revenue-sharing trigger in that because there are legitimate arrangements involved in cooperatives, for example, and the notice for proposed rulemaking recognized this, that could be swept up in a revenue-sharing trigger or prohibition.

We think it would be better to impose a minute-of-use trigger that would address this more precisely and yet sweep any incentives to stimulate access traffic.

MR. BANKS: I wanted to thank the Chairman, the Commissioners, and the staff for their focus on intercarrier com issues and particularly these arbitrage issues and for having the workshops.

Exploiting loopholes in the regulatory access system is a serious problem that siphons money away from communication consumers and communications networks, it raises the cost of communication services and creates complexity and litigation for all companies that involves the federal government, the states, courts, and is a real drag on investment and communication networks and serving communications consumers.

Phantom traffic and access stimulation are the two key arbitrage issues and it's great that this panel is addressing them. Phantom traffic is an issue that springs from the need for billing information so that calls that traverse the communications network can be billed correctly.

Our concern is that service providers have been deliberately not providing that information, or stripping it as it moves across communications networks. And that the Commission's rules don't sufficiently address all the service providers that originate calls and transport them.

The FCC in the recent NPRMs proposes rules that would require service providers to provide the information necessary for billing and to ensure that that gets transmitted across networks as calls flow. We think the FCC's proposed rules go to the heart of the phantom traffic problem by requiring all service providers to provide calling party information and intermediate carriers to transmit that information so that the information flows through to the carrier at the end of the call that can then bill for the services.

U.S. Telecom has spent years working on this and has developed a broad consensus proposal on phantom traffic. It has additional safeguards built into it that we urge the staff and the Commissioners to consider. In addition, the proposed rules, in our view, requires some narrow technical modifications. However, they take aim at the very heart of the phantom traffic problem and we wholeheartedly support their implementation immediately to help solve this problem.

And let me just say that the phantom traffic and access stimulations solutions need to be implemented now. They would provide better information to all of us on the types and kinds of traffic traversing our networks. They would preserve the integrity of the FCC's access scheme. And arguments that continued delay in implementing these narrow, targeted solutions that continued delay is essential to comprehensive reform have not proven out over the last several years. Not solving these issues does not help do comprehensive reform. These are discreet issues at solving them would build momentum for reform.

And in terms of our membership, which spans the smallest carriers to the largest, solving these problems will not reduce our members's incentives to engage in comprehensive reform, which is a much bigger and more pressing problem. Thank you.

MR. SCHORNACK: My name is Dave Schornack. I'm the Director of Business Development and Sales for IVICK Enterprises, the parent company of TekStar. I'm here with my local Minnesota counsel, Dan Lipschultz. I want to thank the FCC for inviting us to appear before today's workshop. And I would like to make four points in my remarks.

First, addressing concerns about access stimulation requires one action by the Commission, adoption of rules ensuring just and reasonable rates as access traffic volumes increase substantially. Second, the market has developed to address compensation for the termination of high track volumes by rural CLEC. The resulting compensation agreements provide the best foundation upon which the Commission should base any rules. Third, the Commission's proposed solution is appropriate because it reflects these market agreements and the Commission's current CLEC bench marking rules, reduces uncertainty, and based upon our extensive experience is enforceable.

Finally, the Commission should make clear that if a rural CLEC that has entered into revenue-agreements, has modified its tariffs as required by the new rule, a termination of toll traffic on the CLEC network for an IFC is exchanged access service provided to that ISC and the CLEC should receive payment as set forth in the new rule. I believe I can speak for everyone is saying that we all wish to avoid any new rounds of litigation period.

Background on TekStar, TekStar is a facility-based rural CLEC operating in Minnesota since 1997. We provide telecommunication, internet and voice services to approximately 15,000 residential and business customers of which approximately a dozen are call-conferencing entities.

As a rural CLEC, TekStar is entitled under the Commission's rules to assess interstate switched access charges at the Neckband 8 rates, currently over 3.6 cents per minute of use because it competes with a non-rule ILEC.

Even though it is permitted to charge at the Neckband 8 local switching rate, TekStar has market agreements for over three years with many ISCs that range substantially below the benchmark rate TekStar is entitled to charge as a rural CLEC. These agreements now cover approximately 80 percent of the interstate switched access services TekStar provides.

Last year, TekStar filed a new interstate tariff that with a Flex in it's market experience in its market agreements. At the lowest volume band, TekStar's marginal rates are now 50 percent of the rate TekStar is entitled to charge under the current rules. And the highest band, the marginal rates are approximately 10 percent to what it's entitled to charge.

TekStar agreements are largely the result of three factors. First, both ILECs and rural CLECs have incentives to settle disputes. Secondly, the Commission's decision since 2007 that provided important directions to ILECs and rural CLEC about their rights and obligations.

Finally, ILECs refused to pay tariff rates when they suspect thee is access stimulation. As a result, a market has developed to address compensation for the termination of high traffic volumes of ILEC traffic by CLEC.

In essence, today any rural CLEC engaged in determining high volumes of interexchange traffic for its customers and for the ILEC's customers who placed the calls that wants to receive payment from an IFC for the carriage of the toll call traffic on their network has to enter into an agreement with the ILEC at reduced rates, close to what is being proposed by the Commission. So we believe that the Commission is on target in what they're doing. Thank you for your time.

MR. LEWIS: Thank you very much for sharing your thoughts and ideas with us. We'll now open it up for questions. And again, anyone here in the room if you have a question there are note cards available from staff. Please flag one of them down, write down your question, and they'll bring it up here to the panel.

If you're online, the email address is ICCreform@FCC.gov. So Commissioners or Commissioner's staff would you like to start off our questioning? I know that Randy has a question.

(Laughter.)

MR. CLARKE: I certainly do. What a great day. Everybody is here thinking about phantom traffic and access stimulation. Let's take advantage of it and jump right in with some thoughts about phantom traffic.

As you all know, our notice propose to require telecommunications providers and interconnected service providers to transmit calling party telephone number to the next provider in the call path. And some of you mentioned our proposed rules in your statements.

I want to dig just a little bit deeper as to whether or not you think those proposed rules are an effective solution going forward. If not, what would be the most effective forwarding-looking solution? And if we get into another solution, particularly, Mike you started it. If we get into OCNs and JIPs and CICs and all of that good stuff how do we draw the line between necessary Commission rules and effective industry standards?

I guess since I called you out feel free to take the first crack at it, but I'm interested to hear what all of our panelists have to say.

MR. ROMANO: Sure. I think you have to start from the premise of those fundamental questions you're trying to answer. You really do come back to CPN and CN tell you who placed the call and potentially the jurisdiction of the caller, although that's not always the case either.

Certainly though, regardless of what the rate is, we're going to end up in a situation where I may no know who to bill in an environment where the number has been ported or there are other complicated with intermediate gateways and things of that sort. So I think the touchstone needs to be what is necessary for a carrier to figure out who to bill, regardless whether the rate is access or .0007.

And so those acronyms I threw out are some of those that I think the industry has previously identified has enabling a terminating provider to figure out who the responsible, originating provider is. And so passing those through would seem to be an essential foundation.

Beyond that, I think you can certainly leave it open to industry discussion as to whatever fields might serve that purpose or whether one or more of those fields are the right way to go. But you have to have something there to answer that first fundamental question of who do I look to? Because frankly, if I don't know who to look to I probably have to look to the last carrier who handed it to me in line. And I know that that's a concern for some in the industry. But it's sort of like the check clearing process.

If I only know the last person who handed it to me, I have to look to them because they're in a better position to look upstream and figure out where that call came from and enforce against that provider in terms of like an indemnification regime. So I think that's where I would start to draw the line.

MR. FRANKEL: Can I just maybe counter that a little bit. I would discourage you from adding more requirements and regulations that force the industry to go back, modify systems and so on.

This is an antiquated, ridiculous regime anyway. These days nobody in the big picture, certainly end users don't care whether it's a local, an intra-MTX, an interstate and intrastate call. Propagating that further now isn't helping consumers. We don't care. This is an industry internal problem and it's a legacy problem.

If you look at how the Internet works today, and it works great, nobody cares. You don't know where the server is. You don't know if it's an instate IP connection that you've got. In fact, when you bring up a web window, it's pulling information from all over the world probably and it works great. And if we tried to impose the legacy rules that we have in Telecom on the Internet and you had to pay a millicent to Google for sourcing ad, for Mountain View and so much money for somebody else for pulling data from their server in Idaho, we'd go crazy. So don't put more of this rubbish on top of poor old Telecom that's still struggling to remain relevant.

You absolutely should look upstream. If you got the traffic from XYZ ILEC look to them for where you go with your bill. Don't ask the government to impose additional regulations and have the industry add additional fields so that that sort of all be backwards engineered.

I think that absolutely the mechanisms for now, given that we're stuck with it, you have to force carriers to put in legitimate CPN and CN and to not mess with it along the way, and that's what your rules say. But if you can't figure out what the jurisdiction of the call is, then use factoring.

And by the way, look at wireless. The Telecom world today is dominated by wireless. There are twice as many wireless subscriptions as there are wireline. And that's wireline RBOCs, wireline rural LECs, wireline VoIP. Add all of those together it's still half of wireless, and wireless people are roaming. We don't know what their jurisdiction and the world gets along okay.

And by the way, wireless doesn't collect access charges. They can't tariff them. They get along okay.

So let's look at less regulation and less requirements, simplify the stuff, get the states on board with conforming rates so we don't have to worry about all the minutiae that where the billing actually costs more than the carriage of the call.

MR. BANKS: Let me just jump in a little bit. Just to be clear, we're only talking about rules for the PSTN network. We're not talking about this on the Internet. And I think Mike raises some really good points about OCNs and all this. But having spent years working on this and developing these consensus proposals, and we have some extra things we might want in here.

For way too long, we've let the perfect be the enemy of the good when it comes to a phantom traffic solution. And from our perspective, the thing to do is to implement something that will substantially help with the problem. The Commission's proposed rules would do that. I do think they do need some technical modifications to harmonize the feasibility and standard-setting exceptions. Those are narrow and technical, however, the rules themselves would make a substantial step forward and one that we should have taken years ago and one that would have benefitted us all substantially.

I think we need to implement those. We need to pay attention to some of the extra issues we've raised or Mike has raise over time. But getting this done now in the right way would make a big difference, and the Commission's rules are a huge step forward.

MS. NEWMAN: One thing I would like to add is maybe to deal with some of these issues, especially with indirect interconnection were some CLEC carriers refuse to enter into an agreement is you can figure this out if you actually have an agreement. And if the principal of the T-Mobile decision could apply in this case here to carriers or CLECs who do not enter into agreements and let us use that process, which already exist, to be able to establish agreements we would be able to I think figure out all these issues because you'd be dealing directly in an agreement context with them.

MR. FRANKEL: If I might just respond briefly. The problem here is I think we've got a little bit of a whipsaw. I mean David says on the one hand I should look to the carrier who just handed to call off to me, but on the other hand, under the current rules, I can't to the carrier who just handed the call off to me as the terminating carrier because I'm supposed to look to who the carrier is that's responsible. Right now there's been a lot of debate in the industry over whether a transit provider or the tandem provider should be responsible for terminating compensation and then turn around upstream.

So while David's solution sounds good in theory, the fact the rules don't work that way right now. So I really do need to know who the carrier is who's financially responsible for that call to pay me for it through the kind of information I talked about, or in the alternative impose a regime along the lines of what David just said. But you've got large carriers who perform very significant tandem functions who oppose that kind of a regime. So it's a bit of a whipsaw to say we've got to move away from that without changing otherwise the compensation structure.

MR. BANKS: I think what Melissa is

proposing is a solution to that problem. The Commission's rules are clear that the originating carrier is responsible. The issue for our smaller members like Mike's is oftentimes they get traffic through a tandem or an intermediate carrier and they don't have a contract or a billing relationship with a CLEC that originated the call.

Under the Commission's rules, CLECs can make ILECs negotiate, but ILEC can't make CLEC negotiate. So our smaller members when they approach CLEC often don't get anywhere in terms of negotiating a contract that would provide for billing. If we did have an exception to the T-Mobile doctrine and applied that so that small ILECs could essentially force CLEC to sit down at the negotiating table -- they could not force the result, but they could force a good faith bargaining. Then the smaller ILEC could come up with some sort of billing arrangement with the distant CLEC. And with the Commission's proposed phantom rules would have enough information to start the bargaining process.

So that seemed to us after rounds and rounds of industry negotiations to be the sensible approach to this rather than trying to make somebody the banker who goes back to someone else who goes back to someone else.

MR. CLARKE: Thank you for that. We have a question from one of our Web-X online participants, and thank you for your question.

The question is does phantom traffic have to originate on the PSTN?

MR. BANKS: No, phantom traffic can and does originate anywhere. The Commission's rule now require that most PSTN calls have this information. I think the rules may technically not apply to service providers that are IP-originating calls. However, so phantom traffic can originate in a lot of different places. Some phantom traffic originates because of technical issues with certain older switches or transit arrangements or 800-number calling. But there is a substantial amount of phantom traffic that originates on the IP side.

MR. FRANKEL: And in fact, I would argue that phantom traffic is interwoven with the VoIP ICC problem because, in fact, a lot of IP-originated traffic on purpose is labeled such that it arbitrages or games the ICC system. You can see that in the calling patterns and calling data.

MR. CLARKE: I didn't plan to plug for our second panel, but we will be addressing those issues.

MR. LITMAN: To help us receive data-driven outcomes in policies, can you help us to quantify the size of the phantom traffic problem? And relatedly, how has the phantom traffic issue changed in the last couple of years with the rise of VoIP traffic?

MR. ROMANO: I don't have any first-hand data on behalf of the collected membership of NTCA, but I know that one example I think Frontier has done a pretty good job of trying to assess this and I would urge people to look at their comments. They've done a pretty good snapshot test case. I think when I saw their comments were filed the other day they had -- I want to say it was 70,000 minutes a day or something. I can't remember exactly what the number was, but terminating to -- originating from what may have been a few numbers or lines.

So there are carriers who have done a study of the magnitude of the problem. Smaller carriers I think have not necessarily gone back and tried to snapshot it. But I've also heard somewhere that it's roughly 6 to 8 percent I think of traffic based upon some studies from a few years ago.

MR. BANKS: When we did a survey of our members, we came up with higher numbers, over 10 percent for the amount of traffic that arrives without all of the information. However, some of that is legitimately arriving without all the information because it's an 800-number calling or whatever. So I think the 5 to 8 percent is a pretty legitimate estimate of the amount of phantom traffic that results from potentially deliberately stripping the information or not providing it.

MR. LEWIS: We have a couple of questions from the audience here in the meeting room. And they apparently would like to focus on access stimulations solutions.

So the first question is why not let IXCs pass terminating access rates onto originating toll callers and let those originating callers chose to call a free conference bridge or not? Isn't that a workable market solution to traffic pumping?

MR. ERICKSON: I believe that's what's happened. As a Telecom consumer, I'm paying a telephone bills. I'm paying some of my plans per minutes. Some of them are unlimited long distance, but I'm basically paying my long distance company to connect my calls.

The thing here, right, is that we can't differentiate different types of toll conferencing, for example. When AT&T does toll conferencing in

Atlanta, everyone pays their access there, right? The access gets paid. It's a non-geographical application and so it could be hosted anywhere. Why not host it in rural areas and drive some of the revenues out there? So the consumer is paying for termination of the calls. That's what I believe the consumer pays for. If it's not to terminate, if it's not to connect the call, what are they paying for?

MR. FRANKEL: I think what the audience member's question is driving back -- revokes in my mind 900 and 976 calling where it's a premium-based service and the caller would pay an extra charge and know that they're paying an extra charge. And that's the trick here is how are callers supposed to know that they are going to pay a premium to get this premium service at the other end? And we do have 900 numbers and we have 976 numbers, and they don't work very well. And they sort of got into disuse because customers found that a very frustrating environment and carriers found it very frustrating because they were serving as the billers for that.

And I think what does serve consumers today in our country today is we do have flat-rated calling, essentially, to the entire land. And people like that and they like the simplicity of that. And so the dilemma, to answer the question, with passing that back through specifically at differentiated rates is that end users really have a very difficult time with that. Businesses and others that allow people to use their telephones have a difficult time policing that. It puts all the burden on the end user community and they're not prepared to deal with it.

MR. ERICKSON: I'd like to add one more thought to that. Would we do the same with voicemail? Voicemail is an application. If the voicemail is not there, the access doesn't get stimulated. If the voicemail is there, then it answers and picks up and they can leave a message and then access is stimulated, right?

This isn't a normal calling procedure, right? The idea that somehow it becomes different is just -- I don't know where we get there with that, right? It's a telephone call. We're making a telephone call. There's access on every telephone call.

MR. FRANKEL: There is. They're just not differentiated. I mean the differential in the access charge I think is what's often disputed here. And voicemail is incidental to regular telephone service and so unless people are running pure voicemail only services, it's not really analogous. So the question is when you have a service that is very specifically a mechanized termination is it appropriate to have a differential access charge apply in that situation or, in fact, should the opposite be true and should the access charge be either comparable or even less than in a traditional call termination?

MS. TANNER: As one of the panel said, it would require you to actually identify this traffic as 900 numbers. And what we found in the IAB proceeding is that part of the problem is this traffic is not accurately labeled. For example, adult content that should be labeled with a 900 number.

There are federal rules in place that say this traffic needs to be identified. Carriers need to take action to prohibit this content from reaching children. That's not happening. So if you take this approach by identifying the traffic with a 900 number, we're going to create rules to chase down another symptom of this problem and I don't think you're going to get to the root of the problem, which is that you are allowing carriers to receive the higher access rates that were always meant for low levels of use.

And so I think that would be very difficult to actually regulate. I went into the legalities in my opening statements about they found these violated the tariffs. But what the IUB proceeding showed was a myriad of ways that folks have gamed the system and it's hard for us to keep track of it. So I think the best way is just to solve the problem at the source of the issue and not try to figure out what content is what and assigning value to context as Mr. Erickson said. We don't regulate content. Why does this phone call cost more than another simply based on context? That is something that we want nothing to do with at the state commissions.

MR. SCHORNACK: I think the FCC is on target with their whole concept of if you have a revenue-sharing agreement in place maybe that's the trigger. And we've worked through market agreements with many of the ILECs reducing our rates really basically down to in some of our agreements close to the RBOC rates. And so I think it is working out there. We're not monitors or judges of the traffic.

MR. ROMANO: The comment I guess I would have about revenue sharing is that we've mentioned this with the time permitted in the opening statement, but is the concern that it could be overly broad and sweep up legitimate arrangements.

In smaller areas, you've got telcos that have five employees. They're not large companies. And potentially they may be buying more in wholesale long distance service than they are charging in access. And so is that kind of an arrangement revenue sharing? I don't that's the intent, but the ability to comply with that kind of requirement post hoc is hard to do because you don't know what exactly falls within the scope of a revenue-sharing arrangement.

Likewise, cooperatives when they issue credits to members is that a revenue-sharing arrangement? If they pay their electric utility more for electrical service than they receive from service payments in the same area, the electric cooperative in that area. Those are just some examples. And again, I don't think any of them are intended to be swept up by it, but there's a concern that they could be.

One thing we liked in the U.S. Telecom proposal from October -- I say U.S. Telecom, but they filed that it was a coalition of groups who were on that. They had a minutes-of-use trigger and I think that actually is of interest because it gets to the heart of the economics of the issue. I mean you could have a case in which the stimulation of access that isn't shared with anyone. It just accrues to the benefit of the provider who stimulated the access traffic and so having a minute-of-use trigger would get to those types of volume stimulation exercise as well while not potentially sweeping up intentionally other arrangements that are legitimate.

MS. NEWMAN: I just will add to that. As I understand the proposed rules, it's not so much that you couldn't have a revenue-sharing arrangement. It's just once you had one there would then be changes in rates. So it's not saying that they can't exist and that's why I think the trigger is actually a good one. You're not saying it's, per say, unlawful. But you are making changes in the rates to go from there and I'm not sure I see a problem with that because you would still be able to take on legitimate revenue-sharing opportunities.

MR. ROMANO: That's true. But I might only have ten minutes of traffic and my rate has suddenly been shot down and I've got no high volume of traffic. So you've got a case in which you're artificially driving down the rate without any thither to whether there's actually been a high volume of traffic or not.

MR. ERICKSON: This is the reason why we believe that it has to be a two-stage test. The first would be revenue sharing triggers a high volume access tariff, and then volume triggers the lowering of the rate. And with those two tests in place, you protect the company he's talking about that only has ten minutes. They file a high-volume access tariff. They're required to refile, but it doesn't affect their rate because they don't have the high amounts of access to trigger the lowering of the rate. And the company that does stimulate access, right, basically starts heading towards the RBOC rate or the largest ILEC in the state.

MR. SCHORNACK: The thing you want to remember is you want to keep it simple. You don't want to have it burdensome and we be all here again arguing over the rules. And so I think the key is try to keep it simple, not make it burdensome on all of us to be able to fulfill the rules.

MS. NEWMAN: Here's the interesting thing about this issue on access stimulation. There's agreement on this panel to do something to change the rates. I'm fine with the trigger that's been of use, actually. But the surprise to me on this panel, which I hope is some comfort to the FCC is you have really a cross-section of folks on this panel saying you can do something here on access stimulation and I hope that point does not get lost. There seems to be broad agreement up here on that point.

MR. LEWIS: Just a follow-up question from the audience here on revenue sharing. Is the real issue not revenue sharing but sharing the results in payment to the customer?

MR. FRANKEL: In our comments, we tried to come up with some alternate wording I think to address your concern. And that is that the point is that is a particular customer or a partner uses more traffic if that results in the net obligation of that customer towards the carrier going down, including in aggregate, not per minute but in aggregate going down. In other words, the more they use the less their bill is or in fact it may get to the point that the carrier is now obligated to pay them. But if that's the structure of the agreement, then that's an indication that they are getting an excess return from intercarrier compensation to the point that they are able to allow their customer to pay less or to even earn money from them.

And so for your example of the power company, I mean you don't have any legitimate customers where they pay a power bill and also as the power company makes more phone calls or receive more phone calls they pay less to your carrier.

MR. ROMANO: So what you're talking about is not a net payment measurement necessarily. It's literally that their bill goes down as the usage of that customer increases. So it's not the case if a Telco cooperative in a rural area happens to be paying more for its power usage to the electric coop than the electric coop is buying the telecom services. You're saying that kind of rule will not be swept up. I mean that could be something that could work together.

I do think, though, that it still frankly may not sweep up the cases in which you've got high volumes of traffic that aren't necessarily shared.

MR. FRANKEL: But that's the difficulty is how do you impute such agreements when you have under one umbrella an enhanced provider or an enhanced service being delivered and there is no explicit agreement, so then you have to impute an agreement and that obviously gets trickier.

MR. BANKS: Yes. And from our perspective working on this, there is a certain simplicity to the minutes-of-use measurements because they're relatively more public than revenue sharing or access-sharing agreements. But again, to echo what Melissa was saying, this is something where there's a lot of agreement that there's a problem. There is a lot agreement that there are sensible steps we can take soon that would preserve a lot of money that's flowing out from communications consumers and networks and focus that money on investing in broadband.

And again, let's not let the perfect be the enemy of the good and takes some steps to solve this soon.

MS. TANNER: yes, I would agree with that. The IUB was asked, both in the contested case and in our rulemaking docket to make a finding that we would prohibit access-sharing revenue agreements, and we were hesitate to do that. We had a lot of the same questions that the FCC has noticed up -- how do you define it? What if the ILEC itself is conducting the activity? And so we worried about being overly broad.

And so instead what we found was similar to what the panel just say is an access-revenue sharing agreement can be evidence that your access rates are too high. And so that's why we adopted a minute-use-type trigger. It is actually for an increase in your minutes of use. But I have to say I do like the CenturyLink proposal where they just have a set minute of use. I don't remember if that was proposed to us or not in our state rulemaking, but it's certainly much simpler than the IUB approach, which requires a trigger of an increase of 100 percent over six months. And there was a lot of testimony and evidence back and forth and if that's the right trigger. So I think it all comes down to the minutes of use and there are many ways to get there.

MR. ERICKSON: I think that the minute-of-use per line -- people looked to solve something in the rural areas with that, but that doesn't get used in the urban areas and we'd like to try and keep the playing field level.

In Crow Creek, we were able to work with the Native American Indians there who built a tribally-owned phone company, did a revenue sharing arrangement with us, implemented a high-volume access tariff, put it in front of the FCC on a 15-day. It was approved and we started working together. It's been a huge success, right? They have not tapped the government for a dime. They haven't done any USF or anything and they have a tribally-owned phone company.

We did the same thing on Pine Ridge and that's two phone companies on Tribal lands in the last couple of years and there is under ten to start with. So I think there is a good way to solve the pricing problem with a pricing solution. I think that revenue sharing is an indicator. I think it's a good trigger, but I think it should have a high-volume access tariff tied to it and bring it down to the RBOC rate, put everybody at a level playing field and distribute some of the minutes that we have that are being done in these big, urban areas they could be out in the rural areas at the same rates, same to the consumer, except supplying infrastructure, high-tech jobs, Native American phone companies, things like that.

MR. SCHORNACK: I agree with what David had to say is that I think the revenue-sharing model does work as a trigger. I think it becomes awful cumbersome when you start, as we've seen the discussion occur here about the minutes-of-use, that creates I think all kinds of other doubts and potential issues with that.

We recognize, as a company we have, as I mentioned in my comments, we've negotiated with other IFCs for lower rates that are fairly similar to the RBOC and I think that model works. And we realize that as the number of minutes terminated increased that we should reduce our rates and we have done that. And I think that model works. I think it's simple. It's easy. It's not as burdensome as some of the other proposals.

MR. ERICKSON: One more thing I'd like to add. I think the high-volume access tariff is also easy to regulate, right? The carriers know what the tariff is and they know what their volumes are going to that local exchange carrier. Where when it's minutes-of-use on lines and things of that nature, how we regulate that? How do we keep all that reported? How do we make the adjustments? When do we make the adjustments? What happens if people don't make the adjustments? It's a little more difficult to police, in my eyes.

MR. FRANKEL: Just with reference to policing, I think that when we talk about referencing the RBOC rate, we throw that number out very casually. If you go look at the tariffs, there are many, many elements that are included there. And going back to my most-cost routing notion, unfortunately, as someone mentioned, you poke this problem in one place and it pops up somewhere else. And I just think with respect to keeping rules simple I mean you make reference to, okay, that it has to be benchmarked to the RBOC rate. It may be even simpler to simply specify what that rate is so that there isn't all of these different elements and mileage and other things that get dreamed up that then end up being disputes as well.

We're all looking for, as someone said, we don't want to let the perfect be the enemy of the good. We want to try to come up with something that's fairly simple and straightforward. I think whatever solution you come up with it is not going to be consensus. There are people here on this panel that have fundamentally different positions about different aspects of this, so some of us are going to end up being disappointed in what you do. There is no solution that will make everybody happy. You're going to have to go back to some basic principles and then make some hard decisions and say this is the way it's going to be, and recognize, by the way, that these are essentially interim solutions until, by the way, we get the whole system reformed.

MR. LEWIS: Thank you very much. And just one logistical point. It was brought to my attention that if you pull the microphone closer to yourself before you start speaking it will work better.

For those of you have suggested a minutes-of-use trigger, could you help us understand your thoughts on how the Commission could distinguish I will say legitimate increases in traffic volume, for example, Microsoft planting a new call center in the middle of Nebraska with high-call volume increases due to access stimulation arrangements?

MS. TANNER: I think that's the beauty of it. You don't need to distinguish between legitimate and illegitimate traffic. I don't think it matters. I mentioned adult content before and there was a lot of effort to get us pretty excited about that in the Utilities Board proceeding, and ultimately we were worried about it because of the identification issue, but we don't care what people are doing when they make phone calls and it doesn't matter if you're in a BOC calling territory and it's a conference center or if you're in a ILEC territory and it's a call center. It doesn't matter.

And that's another reason why we went to this minutes-of-use trigger in Iowa because we don't want to place a value on traffic and distinguish between what's legitimate and what's not, nor do we care what you do with it. And there's a lot of talk about we do great things with this money. It doesn't matter. As long as your rates are reasonable, it doesn't matter what the traffic is for. It doesn't matter what you do with your reasonable profits.

MR. ERICKSON: I think that it should be a level playing field at the end of the day, urban to rural if you're going to do high-volume access. And I think if you do minutes-of-use it's not a level playing field. So the idea is to create a level playing field and distribute the minutes. It's going to make a healthier network than if it's all the urban areas.

MR. BANKS: This level playing field notion is one that I think Dave Frankel has really taken care of. I mean a level playing field means you put things where the costs are lowest and that's where one would expect these things to go, which would tend to be in places where transport costs are low and there's lots of fiber, so that's what we would expect.

And I do agree with Krista Tanner about this is really not about distinguishing legitimate from illegitimate. It's just trying to keep access charges reflective of costs and volume. So if somebody's volume doubles and we have a proposal that is it a very high increase? If their volume goes way up, then their cost-per-minute go down. And it's just a matter of having their tariff reflect that. So it's not about legitimate or illegitimate traffic. It's just about costs and volume, which is how telecom networks work.

So all of these are triggers, right, and they just start a process to make sure that your rates reflect your costs.

MR. ROMANO: I would agree. And I guess one other note on the minutes-of-use threshold, if one were to use that is that it should be measured over a large enough sample size that you're actually seeing a sustained increase in the traffic rather that something that might be a seasonal spike or something like that that results in the rate going downward and not sure what the path would be for putting it back up again when would requalify to set your rate higher again, potentially, if you're adjusting it. So again, just getting to the definitional aspects of the trigger it's important I think to look at it. We had suggested over a quarterly period before doing any sort of adjustment to just make sure you've got a right size sample.

MS. NEWMAN: I would agree. I would add that it would also be helpful that when you get phone calls asking about why the spike, even if it's a month or two, that you have a dialogue about what's going on so you can identify early on that it's seasonal, or you can identify that it's not and deal with it appropriately. But I echo what Jon Banks said, which it's all about costs and volumes. And the original purpose of these high access rates in rural areas was premised on low volumes. For whatever reason, over a sustained period of times those volumes increase. It requires, in our view at CenturyLink, that you go back and adjust your rates accordingly to reflect the costs because the premise no longer exists.

MR. ERICKSON: I believe that the idea that we have higher rural rates is to sustain the public switch telephone network in the rural areas. And that if we do things to inhibit growth in those areas it's going to be more difficult to sustain and it's going to require more government help to sustain it. And so we work in the urban areas. We work in the rural areas, right, and I would like to see a level playing field between the two. There's no reason to inhibit rural areas to sustain their networks.

MR. ROMANO: If I may just add, I agree and that's why defining the triggers carefully becomes so important because you've got to make sure that you're not picking up false positives or being overly aggressive in driving the rates downward in a way that doesn't reflect or inhibits cost recovery for operating in what are the highest cost areas in the country. So that's why I think the definitional triggers become so important.

It's also important from a compliance perspective so that companies know in advance what it is they need to do and where they need to be with their rates at a certain point in time rather than having a speculation as to am I sharing revenue, am I not? How does this arrangement fit into the picture? Having precision in defining those triggers I think will help in addressing the concern about cost recovery in rural areas as well as compliance issues.

And frankly, at the end of the day for us too it's also important to us because we need carriers to start paying their bills rather than disputing them over suspected access stimulation. I mean in some ways the long distance market has become the Wild West. People are disputing bills left and right. They're refusing to terminate calls to long distance areas. They're affirmatively ceasing in some cases the delivery of those calls or delaying them.

Getting this issue out of the way and clearing this underbrush will go a long way towards getting the PSTN working again.

MS. KROENBERG: Mr. Erickson, I'd like to follow up on something that you just said.

Where do we as the Commission draw the line between sustaining the rural areas that need assistance through the Universal Service Fund versus through the ICC regime?

MR. ERICKSON: Where do you draw the line?

What I know is that on the Native American Territory they didn't have to use any USF at all and I like that and they liked that, and they prefer that. And that's possible through a high-access tariff. And it works. And it's in the wholesale marketplace today and it's a vibrant wholesale marketplace. And I don't see why that shouldn't be an option.

MR. BANKS: Andrew, I think it's a great question. Today, USF and ICC work in tandem to support universal availability, the ubiquity of telephone service at affordable rates, which is sort of a social mandate that we have. and I think we all want to move to explicit subsidies.

MS. KROENBERG: And didn't Congress tell us to do that in the '96 Act? I know Jonathan has opinion about that.

MR. BANKS; Yes, Congress told you to do that. It's a bad idea, from our viewpoint, to continue this implicit subsidies in access rates. Everybody's goal I think is to have the same rates across the country, urban and rural, and move all those subsidies into a broadband fund that we say here are some broadband dollars. Build some broadband and not have it depend on this implicit maybe there's money in some access rates in one carrier, but not in the next carrier. So access rates should be very low and subsidies should be in USF with explicit obligations.

MS. TANNER: Angela, I'd agree. And to me not only are the comments about what you do with your profits is irrelevant too if this is the appropriate charge. I think it is an admission that these are subsidies. And I don't know about you, but when I have carriers come to talk to me about intercarrier compensation reform they talk about costs. They talk about costs, but they're really talking about the cost of their broadband network. They're talking about the cost of running their company and they're about subsidies. But when I call it a subsidy, they get very upset. But I think the important part these comments it is an admission that we all know that these are subsidies. And as you noted, there's a place for those and that's the Universal Service Fund, not in your intercarrier compensation.

MR. ROMANO: And I don't think anybody disagrees with that. It's just a question of a transitional mechanism. I mean one could look at it and say why are we here talking about access stimulation because it's all going to go away once we've reformed and moved to a broadband world.

The fact is we're dealing with it because until we get to that broadband world we have to deal with the hand we've been dealt. And so I think you're right. I think ultimately I think that's where the end game is, if you will. And I think we do end up with, hopeful, a universal service mechanism. Today, there's a three-legged stool in terms of intercarrier compensation, universal service support, and end user rates that make up the revenue and cost recovery streams that support a rural carrier operating. Ultimately, it may be a two-legged stool for lack of a better way of putting it because you're going to have universal service and end user rates.

But until the rest of their long-term reforms occur, we do have to deal with it as how do we get the right level of support built into this implicit mechanism without setting up incentives or eliminating or at least curbing the incentives that result in practices that we would deem to be uneconomic or beyond the appropriate level of support. So I think that's where this debate comes in.

MR. LEWIS: Dealing with the world we have today, what about the very large unpaid amounts, amounts in dispute with current high-volume access providers? Are the current high-volume access tariffs lawful? And I guess maybe a discussion of what the experience has been in Iowa?

MS. TANNER: I can talk about Iowa, and we found -- now it's a little different from the FCC. Not that the tariffs weren't lawful, but that the traffic at issue was not traffic subject to compensation under the tariff and so those amounts paid pursuant to the tariff were paid in error or not legitimate payments and they ere due to be refunded.

And I think Melissa noted earlier, if it's a fraudulent tariff, which is a different question, then no it should not be given a deemed lawful status.

The unfortunate facts that were found by the IUB were that -- we're talking about this in very benign terms, levels of minutes-of-use and appropriate rate, but the reality is that these schemes -- and I use the word "scheme" are far more sinister.

In our proceeding, we found that the parties had falsified documents to the FCC and the Utilities Board to make it look as though they had always been end user customers. We found that some ILECs were assessing access rates even though the traffic did not even terminate in their exchange. It terminated in their affiliated exchange because they had over 13 minutes a minute of access and so that tariff should never apply to that traffic.

And we also found instances were carriers were in an urban area, but they put equipment in an non-rural area, said that they were serving a rural exchange so they could apply the rural exemption.

There is another, and this is not related to access charges, but one of these traffic pumpers were using their free conference-calling lines to collect universal service dollars. They weren't even in a rural exchange. And so my point is, is that when that sort of fraud exists, the tariff is off the table. The tariff either doesn't apply or if the tariff is used to perpetuate a fraud that tariff should not be deemed lawful and that's how I feel about that.

MR. SCHORNACK: We have to be very careful to make sure that we don't paint everybody with the same brush that happened in Iowa. I think that our tariffs are lawful and we've been able to negotiate with our IXCs. The IXCs evidently view that as terminated access. They bill their end user for that access. They treat them as access, all of that traffic as far as they're concerned. And we've been able to negotiate contracts with the largest IXCs in the country. And so I just want to make sure that we just don't paint everybody with the same brush that's in this business that occurred in Iowa because I don't think that's universally true.

MR. TANNER: I agree with that. I'm just saying when it happens you don't get the protection of your tariffs?

MR. SCHORNACK: And that's okay.

MS. NEWMAN: What she said.

(Laughter.)

MS. NEWMAN: I was not involved in the Iowa proceeding. There was a lot of material that was confidential and I am not privy to the exact details of the fraud there, but we did know that that is going on and it is what prompted CenturyLink and I'll say Classic Quest at the time to really go forward with this full throttle. And in our view it is exactly what Krista said, which these are tariffs. The access should not even been applied in the first place. The tariff doesn't apply and the issue is appropriately in litigation.

MR. ROMANO: If I might say, I think this highlight the importance of consequences built into the rule rather than having them be something that has to be enforced outside of the rule. And actually I think the examples that Krista Tanner brings up, as I think the gentleman from TekStar said too, they're not typical of the operations of most of these companies or the vast majority of them. There may be a handful who entered into this, but we don't make policy I think based upon the worse of the bad actors. We set up a rule that all can comply with, know what they're going to be complying with in advance and can be enforced against those who do violate it.

Not to bring it back full circle, but I think the same kind of reasoning needs to apply in the concept of phantom traffic. I mean phantom traffic is very similar. I mean some people called it theft. It's something were someone is deliberately removing information. In one case, people are deliberately driving up their traffic volumes the argument is to stimulate receipt of monies. In the other case, we've got people deliberately removing information to avoid the payment of monies.

Is a very similar dynamic and we could look at the worst actors there too and potentially throw some stones. But I think the point, bringing it back to phantom traffic, would be to build something into the rule just like you're talking about in the access stimulation context that would allow one to enforce the rule without having to go back and file a formal complaint against those that did not pay, to have some consequence built into the rule.

So I just wanted to dovetail back to that and say they are two sides to the same coin and there's a reason why we have them together on this panel I think.

MR. FRANKEL: With respect to, for example, that point about phantom traffic does it make sense for the industry to not terminate calls, not accept calls that are mislabeled? Is that enough push back to stop that from happening?

MR. ROMANO: I don't think we want to have a mechanism built into the rules -- I'll leave it to the Commission to decide what they want to do, but to have people start unilaterally deciding when they will block traffic I think the decision already has been made several times over that that's not a laudable public policy objective to have unilateral determinations about when to block the traffic because I don't think someone is providing adequate information. Rather I think you ought to build into the rules a mechanism that encourages a party to provide that information and sets forth a consequence to the extent that they do not.

MR. FRANKEL: I guess that was my proposed consequence.

MR. ROMANO: The consequence would be economic, just as it is as we're talking about in the traffic stimulation context rather than having people throwing up their own artificial roadblocks on the PSTN.

MR. LEWIS: We're going to conclude this panel at 11 o'clock to give everyone a 15-minute break before the next panel starts. So perhaps one final question.

Under a per minute of use per line volume mechanism, couldn't the local exchange carrier simply add more lines to reduce their volumes per line?

MR. ERICKSON: I think that would be the case, right? I think as we're talking here we're finding out that there's a certain percentage of people that are always looking to bend the rules somehow someway. That's why I like the high-volume access tariff because it's the IXC that's paying the bill that's able to police what's going on in the amount of volume that they send. And the idea that we could take rural phone companies that apply for a rural exemption and make them non-rural exempt phone companies, basically get them down to the RBOC rate is a great idea, right?

The idea of subsidies and all of that

that's what we're trying to get away from. And so if we do it based on volume of traffic, the IXCs can measure it. The IXCs can adjust their price and the rural phone companies becomes a non-rural phone company, so to speak.

MR. BANKS: I think that, yes, companies could add more lines. I mean to the extent that people add more customers they should have higher volumes, but I would like to echo what Commissioner Tanner said is we're not talking about small volumes here. We're talking about huge increases that are really beyond the ability of any small, rural company to add enough lines to bring the huge volumes down to a typical average minutes-per-line.

MR. LEWIS: If there are no further comments, thank you all very much. This has been very helpful and we are looking forward to the next session. Thank you. We'll take a 10- to 15-minute break, starting at exact at 11:15.

(Whereupon, a short recess was taken.)

MR. LEWIS: Will Session 2 panelists please come up?

MS. GILLETT: Good morning and welcome to the second session of the ICC workshop today to talk about the treatment of VoIP, Voice Over Internet

Protocol for purposes of ICC. I'm Sharon Gillett. I'm Chief of the Wireline Bureau and I'm moderating today's panel.

On February 9, the Commission issued a notice of proposed rulemaking that would propose to determine the treatment of VoIP for purposes of ICC. And not having determined it in the past has actually lead to considerable disputes and litigation. And so our proposal in the item was to settle this issue once and for all.

Although the NPRM does not single out a particular proposal, it does outline options for the treatment of VoIP, ranging from VoIP being treated like all other voice calls to applying a VoIP-specific rate to applying bill-and-keep to avoid the calls. And comments came in on Friday, April 1, and we received I believe at last count it was 84 comments, although it may have gone up since then. so I'm expecting a lively discussion from our distinguished panelists today.

And I can tell you from having reviewed the one-page summaries that the panelists were kind enough to supply to us of their comments that all three of those positions and the whole spectrum of positions that were outlined are represented on today's panel, so I think it's likely to be a pretty lively discussion.

We'll take the same format as the last panel. Each panelist will give a three-minute opening. And I must say I really appreciated the last panel sticking to those big red numbers there. Our last panelists were very good to sticking to the timing. Let me introduce the panelists and encourage people to put their comments on to note cards and they'll be delivered over here and we'll ask questions as well as taking them from the online participants.

So our panelists today are Eric Einhorn, who is Vice President of Federal Government Affairs from Windstream Communications, Kathleen Grillo, Senior Vice President of Regulatory Affairs for Verizon Communications, Julie Laine, Group Vice President of Regulatory for Time Warner Cable, Brendan Kasper, Senior Regulatory Counsel for Vonage America, Lisa Youngers, Vice President of Federal Affairs for XO Communications, Inc., Paul Gallant, Senior VP and Telecom Analyst for MF Global, the Washington research group. And last, but certainly not least, Peter McGowan, who's general counsel for the New York State Department of Public Service. And joining me as questioners, I'd also like to acknowledge Angie

Kroenberg, who's remaining with us and I'm sure will have a question at some point for our panelist as well as Marcus Maher. All three of these folks are in the Wireline Bureau. So I'm going to, in the interest of time, skip all the titles -- Marcus Maher, Rebecca Goodheart and Victoria Goldberg, who all work on our intercarrier comp issues here in the Bureau. So with that, Eric, take it away.

MR. EINHORN: Thanks. I'd like to thank the Chairman, Commissioners and FCC staff for holding these workshops and for inviting me to participate today. I think one thing we can all agree on is that the current USF and intercarrier comp system is broken and needs to be fixed. And Windstream has been an ardent supporter of rational reform and moving to a unified rate for all types of calls, including VoIP in conjunction with a reasonable opportunity to recover revenues reduced by the reform.

The FCC should encourage the development of innovative services such as VoIP, but not a manner that undermines investment in the networks used to deliver these services.

Most providers are paying applicable intrastate and interstate access charges today for traffic that terminates on the PSTN. This includes

VoIP. I want to stress this. The vast majority of VoIP-originated traffic is paying jurisdictionalized rates today. However, a small handful of large providers have recently become more aggressive about claiming that VoIP-originated traffic is somehow different and should pay its own special super low rate, a self-declared discount, if you will, based on new claims about uncertainty in the law.

These particular VoIP providers are abusing the network on which they rely and claiming an unreasonable advantage over their rule-abiding VoIP and non-VoIP competitors. And doing so is contrary to existing FCC rules regarding the termination of traffic on the PSTN.

There's no rational basis for treating VoIP and other PSTN traffic differently under the current rules. Both use the same network component, terminating carriers incur the same costs. And from a customer's perspective, these services appear virtually identical and are marketed as substitutes.

The FCC must make it clear that its rules apply to VoIP providers placing on traffic on the PSTN and that they should pay the same rates as all other voice providers and voice traffic. If the FCC doesn't act now, the self-help very well may destabilize the current system before rational reform can take place and undermine the ability of carriers of last resort to serve consumers in high-cost areas. This is will harm consumer rather than help encourage broadband deployment.

Allowing VoIP providers to arbitrarily avail themselves of a lower rate is a different kind of reform. It's reform dictated by a few actors rather than rational reform with reasonable transitions that the NPRM envisions.

Windstream has and will continue to work with the FCC, the states, and others in the industry from all sides to develop a path forward on these important issues and we look forward to doing do.

MS. GRILLO: Thank you for the opportunity to appear here today and discuss these issues. I just wanted to start by extending a compliment to the panelists and the staff from the first panel. I thought it was very good, very interesting. And you know in a lot of these discussions we tend to all retreat to our respective corners and I thought that was a very good dialogue and very substantive. So I'm looking forward to the same experience here today.

The Chairman and the Commissioners have been very clear that reforming universal service and intercarrier compensation is one of their top priorities for 2011 and that is welcome news to Verizon.

Virtually every player in this debate agrees that these systems desperately need reform. I actually wrote down that the Commissioners and panelists used to describe the current system and some of them were byzantine, broken, tangled, antiquated, and inefficient.

On the intercarrier compensation side there are a host of problems that we need to address, but the most immediate and the most in need of Commission action is the issue of what compensation carriers pay to each other when exchanging VoIP traffic from the circuit switch network. This issue has tied the industry in knots for years. It districts from other priorities and it drives carriers to litigation and disputes.

The Commission can put an end to these problems now by establish a default rate for VoIP PSTN traffic. But Verizon believes the industry can solve most of these issues through commercial agreements. We have asked policy makers not only to endorse commercial agreements, but to encourage them.

Commercial agreements give carriers the

flexibility to take account of their individual circumstances and traffic flows and reach mutually agreeable terms. In the absence of these agreements, the FCC should set a default rate. We have suggest .0007, which is a rate the wireless and wireline carrier exchange for a lot of different traffic today.

So we have a large group here today and I'm sure we're going to disagree on many things, but I think we'll all agree that this is an issue that needs to get decided quickly, preferably very soon. It's a problem that's only going to get worse over time and we've seen this before in other context and I think we're seeing it now. The more these traffic volumes increase and the more disputes we have the problem is only to get worse.

So again, I look forward to discussing this issue with all of you today.

MS. LAINE: Good morning and thank you for the opportunity to appear her to share Time Warner Cable's views of this important topic.

Time Warner Cable believes that the fundamental goal of intercarrier compensation reform should be harmonize and simplify the current system in a manner that is technologically and competitively mutual. As long as the rates that carriers pay and collect are based on artificial regulatory and jurisdictional distinctions there will be continuing incentives to game the system.

And we therefore believe that with respect to VoIP services, as the Commission has acknowledged, similar services should be subject to similar rules.

First, telecommunications traffic terminated by LECs should be subject to the same intercarrier compensation rules regardless of the technology used by the originating or terminating carrier. The NPRM does not define the term VoIP traffic. And in fact, the term as used is misleading.

The Commission appears to consider VoIP traffic to encompass any interconnected VoIP traffic on an interconnected VoIP provider's network. But the use of the term confuses the provision of exchange access service by a local exchange carrier with the provision of a distinct retail interconnected VoIP service by a retail provider.

As the NPRM acknowledges, the Commission has already determined that interconnected VoIP traffic is telecommunications traffic based on the pure transmission of the finished service, regardless of whether the end user VoIP service is classified as a telecommunication service or an information service.

Therefore, Time Warner Cable believes that any interim step towards fundamental reform of the intercarrier compensation system should confirm that reciprocal compensation for local calls and access charges for toll calls should apply to traffic delivered to terminating LEC, regardless of whether the traffic originates in circuit switched or IP format and regardless of whether the traffic is ultimately handed to a VoIP provider for termination to an end user customer.

Second, new artificial distinctions amongst types of traffic would hinder the Commission's long-term goals in this area. Without clarification that traffic originating on or terminating to IP-based networks is subject to the same rules as any other telecommunications traffic some carriers will continue to exploit artificial distinctions in traffic or ambiguity in the Commission's rules to reduce or avoid their intercarrier compensation obligations.

Finally, the ESP exemption does not permit IXCs to avoid paying access charges to LEC. Even assuming that interconnected VoIP is an information service, the EXP exemption would not relieve IXCs or LEC from their obligation to pay intercarrier compensation for traffic they deliver to terminating carriers.

As I mentioned earlier, it is not interconnected traffic that is the subject of this debate. It is intra- or interstate access service, which are telecommunication services. Under the Commission's rules and comparable state authority, users of those access services are obligated to pay and providers of such services are entitled to collect intercarrier compensation charges associated with that traffic.

Again, I thank you for inviting me to speak today and I look forward to your questions.

MR. KASPER: Good morning. Thank you for inviting me to discuss this important topic. Before I launch into what we believe the correct approach is, I'd like to explain a little bit about how Vonage fits into the intercarrier compensation system and also how other over-the-top interconnected VoIP providers also fit into that system.

Unlike the carriers on this panel, we're sort of an indirect participant in the intercarrier compensation system. We pay telcos to take traffic to terminate on the PSTN and to receive traffic from the PSTN and often do not have an end user or a relationship with a terminating carrier. So that means that our pricing model is to recover our costs through our end user prices only and not through intercarrier charges, which is important background into why we think that bill-and-keep is the appropriate solution for intercarrier compensation for VoIP.

Bill-and-keep is an important step towards long-term reform. As the NPRM recognizes the Commission is seeking to eliminate non-cost based distinctions driven by jurisdiction and other distinctions. If we fail to specify that VoIP should be subject to bill-and-keep, we will harden the carrier's dependence on intercarrier charges and only make it more difficult to achieve long-term reform.

Second, that VoIP is subject to bill-and-keep promotes a transition to IP networks by eliminating the incentive to funnel traffic through the PSTN in order to maximize intercarrier charges. Third, bill-and-keep is an economically efficient solution. It recovers interconnection costs through end user prices. End user prices like Vonage's price for service is subject to robust competition.

In contrast, intercarrier charges essentially require regulation no matter how competitive the end user market is. Also, bill-and-keep more accurately reflects the benefits received from the call. Traditional calling party network pay solutions posit that the calling party generates the costs or receives a benefit and therefore should pay the cost. But in reality, most communications is two way. Both parties receive a benefit.

And finally, bill-and-keep minimizes the need for ongoing regulations because, as I discussed, there is no need to regulate intercarrier charges.

Thank you and I look forward to your questions.

MS. YOUNGERS: Good morning. Thank you for having me here today to share XO's viewpoint on intercarrier compensation reform and a special thank you to staff for putting together these workshops and providing an opportunity for all of us to be heard on these issues.

The FCC and the industry as a whole has been dealing with intercarrier compensation issues for quite some time and XO looks forward to working with the Commission and its industry peers on resolving these issues expeditiously.

While examination of these issues complicated and there are many moving parts, XO agrees with the other panelists that the time to address intercarrier compensation is now.

We are here today to discuss specifically the appropriate compensation framework for VoIP traffic. It may be helpful, however, briefly to put this all in context and look more broadly at where XO believes intercarrier compensation reform should be heading overall.

Last fall, XO put forward a plan for intercarrier compensation reform on the record, outlining what we believe is the appropriate framework for intercarrier compensation going forward.

Essentially, XO believes a comprehensive intercarrier compensation scheme must be forward looking and include policies that focus on IP networks rather than circuit-switched TDM networks. This is because IP networks provide more efficient and lower cost transport and exchange of traffic.

The bottom line is XO developed an intercarrier compensation plan that mirrors where telecommunication networks are heading. The central piece of that proposal is that IP interconnected should be encouraged, regardless of the technology used to serve particular end users. Adoption of strong IP interconnection policies within the intercarrier compensation regime will create the proper incentives to spur additional broadband deployment.

Therefore, XO proposes that the FCC adopt rules that require carriers to exchange all traffic, whether IP originated or not in IP format within a five-year period. More details of our plan are on the record now and will be filed on April 18 with the rest of the comments regarding comprehensive intercarrier comp reform.

But the question here today is obviously about VoIP and what the FCC can do now with respect to the treatment of VoIP traffic. Last Friday in our comments, XO put forward what we deem as an interim solution for the treatment of VoIP traffic. This solution is interim, of course, only until the FCC adopts a more comprehensive intercarrier compensation scheme.

XO's proposal would apply to all traffic, including VoIP until the treatment of VoIP traffic would be address under a more permanent solution. Specifically as to VoIP, there has been too much uncertainty for too long regarding the treatment of VoIP and what is the appropriate compensation scheme. As such, XO proposes that prospectively VoIP traffic should be treated as a separate category of telecommunications traffic that is not subject to switch taxes charges and that recip comp rates should be applied on an going forward basis when carriers exchange VoIP traffic on a TDM basis.

The FCC has the authority to regulate the compensation for VoIP exclusive and should implement this interim solution immediately.

I look forward to discussing these issues with all of you.

MR. GALLANT: Hi. I'm Paul Gallant with MF Global. Thank you for the opportunity to join you today.

What we do is we provide research to Wall Street about what's happening in Washington that may affect the telecom sector investors interest in stock prices or bonds and the USF issue. Wall Street's primary interest is in the rural phone companies, so I'll mainly talk about the issue through the context of what it means for the rural phone companies and how Wall Street would like this to play out.

The first issue is simply that institutional investors are anxious for reform. For the past four or five years, the Commission has sent conflicting signals about whether it was going to reform the USF and ICC process and what steps it would actually take in course of reforming those rules. And if you look at the stock price reactions to the FCC signals, you see that Wall Street definitely cares about this issue and it is a material issue to Wall Street and I think that Wall Street is glad to see that the FCC is sending signals that it cares about what Wall Street thinks about this issue because there is a place in this debate where the rubber hits the road in terms of the cost of capital that ILECs need to raise to build up broadband in the direction that the FCC wants them to go.

So the first question that we get from investors over the past six to nine months since the broadband came out, or the past year is not what is the FCC going to do to the ILEC, but is the FCC going to do anything because the bits and starts on this issue for the past few years has been a little bit frustrating to Wall Street. So I think it's very encouraging that the Commission and the Chairman and the Commissioners put out a blog post saying we're going to get to this issue hopefully in the next six months or so, so I think that is inspiring some confidence on Wall Street that this issue will be resolved. And that's important and I think that's point one.

The second point is that VoIP within the context of USF and intercarrier comp is a really important issue. There was a lot of Wall Street interest in the national broadband plan last year because of the likelihood it was going to talk about a framework for reforming USF and intercarrier comp. And I think Wall Street reacted positively to both the substance and the tone of the national broadband plan and how it talked about this issue because it had discussion of transition plans and phasing and a sensitivity to the financial realities of the companies that are receiving this money today.

And I think VoIP has the potential, though, to be a bit of an X factor in how the FCC completes this transition process because there are certain approaches within the framework of the NPRM that would have potentially fairly negative consequences for the ILEC and their ability to go to the market and borrow money and expand broadband. And we can talk in a little bit more detail about how each of those approaches I think would be viewed by Wall Street. But I think the broad spectrum of issues or options that the FCC laid out in the NPRM on VoIP are a pretty important and potentially dramatically different path than what the broadband plan was anticipating.

MR. MCGOWAN: Good morning and thank you for inviting New York. I applaud the FCC's efforts and I think there is a lot of momentum behind the effort to reform intercarrier compensation. It's pretty clear to me it's going to happen.

I'd like to just address a couple of remarks from the perspective of trying to manage the reform because that's what we're doing. In New York, we have a docket that's outstanding now where we're attempting to generically for the state develop a new system that will reform, get to the FCC's goal. I think it's our goal as well.

I think there are three reasons for reforming the legacy access system. One is the cost structures are changing. IP is introducing a completely new cost structure. The trends of traffic moving away from the legacy regime are clear and suggest that the legacy system simply isn't sustainable, so we need to focus on the transition.

And thirdly, where an interexchange provider operates in an affiliated manner with a long distance provider I think it's clear that the above cost access regime continues competitive inequities via cross-subsidization through contributory rates.

Access charges are priced well above cost and it's my view that creating a definitive glide path to more rationally price intercarrier compensation actually gives the LEC to move to more efficient IP platforms and develop a sustainable business model. They will either get to a more effective and efficient cost structure or they will not. And they will probably not be sustainable in the long term anyway. And there are a lot of competitive carriers who are entering into the markets who may take over where they are unable to continue.

So in thinking about the problem of reforming the legacy system, let me just center on three points. First, as I mentioned, the costs are changing. We're going to get to a lower cost structure, so we've got to get there.

Second, where intercarrier traffic is exchange on an integrated basis with a long distance provider if there's a symmetrical rate being exchanged, then a reduction in access rates should be less painful financially to the carrier. The loss of access revenue would be offset by the long distance carrier's reduction in access costs. But a lot of local exchange carriers in New York and I think elsewhere are going to be stressed, are stressed now and will be further stressed as the access revenues diminish.

So as we transition, I see the VoIP providers as in relatively good financial shape. They are no longer the nascent technology which needs regulatory protection. But LEC, on the other hand are stressed financially and in limited areas they are the only provider. So we need to recognize that we need reform, but I see the definitive path to lower access charges as an incentive for the LEC to invest in and gravitate to the more cost-effective and sustainable IP network.

VoIP traffic should be subject to the legacy regime with carrier access and reciprocal compensation. Many VoIP carriers, as we're hearing today on the panel have been able to do that and have been able to successfully enter the market. To the extent VoIP carriers resist the legacy system, I see it as part of the cost of the transition. And the most important thing -- I think the priority today -- the Chairman indicated the priority is to reform the access system. We are in New York -- many states have already done it -- we are reforming the system.

We need as many tools as possible to help us get through the transition. To the extent some VoIP providers are not going to contribute to the access regime is going to make the transition all the more difficult. So we want a reform, but we need as many tools as possible to help us get there. Thank you.

MS. GILLETT: Thank you all for your comments. And I'd like to start off the questioning with a question for Paul.

First of all, I just want to point out that we always have to be clear about our terminology here at the Commission. And you used a couple of terms that I think Wall Street interprets somewhat differently than from regulatory folks. One of those is X factor. Some people in this room have a very specific meaning of that term than people who actually construct price CAP regulations.

Seriously though, to clarify what you mean by rural carriers. Here at the Commission rural carriers encompasses about 800 holding companies, most of which are not public. I think you're largely referring to a company like a Windstream, a mid-sized carrier, is that correct? Is that right?

MR. GALLANT: That's right.

MS. GILLETT: Okay. And the question for you was you mentioned that the different proposals in the NPRM might be reacted to differently from Wall

Street. I wondered if you could be more specific. In particular, the NPRM laid out a spectrum from the bill-and-keep idea, which we heard Vonage supporting, the VoIP-specific rate idea, which we heard I think in slightly different forms from Verizon and XO. And then the idea that VoIP is exactly the same as existing traffic, which I think we heard from Windstream and Time Warner. Could you speak a little bit about how investors might react to that spectrum?

MR. GALLANT: Right. So on the option of interconnected VoIP providers paying the full access charges today, I think that is really the only option that would actually improve the stability and the predictability of the rural carriers access charge revenue stream that really helps give confidence to lenders that they can keep lending money to ILEC at a reasonable rate. Either of the other two options, the bill-and-keep option or the set a VoIP-specific rate option tend to, I think, potentially replace one set of or one arena of uncertainty with another in a sense that it's not immediately clear whether the originating -- if the originating carriers have the ability under a bill-and-keep regime or a VoIP-specific rate regime to determine what is VoIP traffic and what is not VoIP traffic.

there is the potential for under certain, depending on how originating carriers behave, the potential for a significant reduction in access charges. And the consequence of that, if that were to play out and I don't know if it would. But if that's how things play out under either of those options, if the Commission goes that way is for Wall Street to look at that and say these access-charge revenues are not predictable any more and we are going to adjust downward our models to reflect that and we're going to charge ILEC more to borrow money to build broadband.

And even in extreme cases, even money that the ILECs have in the pipeline to build broadband today could potentially be subject to repurposing either for share buy-backs or whatever and that's obviously not the direction the Commission would like to see ILECs go, but this is a fairly predictable revenue stream that, again, under certain scenarios of either bill-and-keep or a VoIP-specific rate would introduce even more uncertainty I think into Wall Street's view of these companies than we have today.

MR. MAHER: Maybe just following up a little bit on the aspect of VoIP-specific some of the concern that might arise under either a VoIP-specific approach or a bill-and-keep, and as a question I'll start with

Lisa, but any of the other panelists as well that are suggesting either a VoIP-specific or a bill-and-keep approach.

To the extent that some of the uncertainty comes from the potential uncertainty about what traffic will be treated as VoIP, are there approaches that you see to identifying that in a way that I think would give comfort to the terminating providers and others that there's a way to identify. Here's the traffic we're talking about. There is maybe some certainty then about what the universe of traffic over some time period that's going to be under one particular regime versus another.

MS. YOUNGERS: So XO's position, of course, is that VoIP should be subject recip comp. And your question is about how do you identify that VoIP traffic. And in our comments we talked about that VoIP traffic should be designated up front at VoIP either by agreement -- there are agreements in place that dictate how this is done with carriers or through some sort of industry standard. So some examples and possibilities are one way to do it is having originating carrier populate the JIP, the jurisdictional indicator parameter, which would identify it as VoIP traffic or you could use some sort of factor on the back end. Factors, of course, are done today. You could come up with some sort of factor that works.

XO is also open to any other mechanism that might work or might be agreed to by the industry. We're open to other ideas. So the originating carrier would have to self-designate. And then in our comments we suggested that the terminating carrier would have some sort of audit right, some sort of audit ability to verify that, indeed, the originating carrier is identifying the traffic correctly. And if they are not, there should be some sort of recourse for that. So for example, charging access if it really isn't VoIP.

MR. KASPER: So we actually had a fairly similar proposal. We think that the traffic should be identified as VoIP in either the billing information or the signaling information. And because we're not a carrier we're not entirely clear what the best candidate is. But one thing we saw was that from the IP to PSTN gateway you can populate the calling party category, which is a designation on the PSTN side and be populated with information from the IP headers and then we would suggest that you include that in the phantom traffic rules that you couldn't falsely populate traffic as VoIP that is not VoIP.

MS. GRILLO: Yes. I mean, I don't know if there is much more to add in terms of that. I mean, Lisa said it really well. And I guess another part of this discussion that comes into play when you talk about markets, how would you tell VoIP from circuit-switched traffic, the sooner we move to a comprehensive reform where there's a single rate for all traffic the less -- obviously, there are ways that carriers do that do that today in the wireless space and those could be extended to VoIP traffic. But I think that the sooner we move to deal with these larger issues the less of a concern that really is.

MS. GOODHEART: Just to follow up, Kathy you recommended moving to commercial negotiations and so part of the question comes from the audience is how do the commercial negotiations work when there might be an unequal bargaining power? And also how would the backstop work when negotiations break down? And also, I'd like to open this up to Peter when Kathy is done to talk about what was the experience in New York with the 2008 decision which encouraged parties to negotiation a commercial arrangement for the treatment of I think Vonage's traffic. And so if you could speak about how that worked as well.

MS. GRILLO: I mean commercial agreements work in many different context between many different players. In fact, as David was saying on the first panel that's how the Internet works today.

And I don't know exactly what you mean by unequal bargaining power. I think people can use that in different ways and in different contexts. But I know from our perspective when we're negotiating with carriers the focus is on a reciprocal arrangement. So there's a quality in terms of what one carrier pays and the other carrier pays for VoIP and a lot of times we end up at a rate that's lower than .0007, frankly, in a lot of cases.

So I mean I think they work well in a lot of different context, especially when both parties are motivated to get something done and to bring it out of the regulatory regime.

MR. MCGOWAN: I guess the problem of the balance of power might be evidenced when a carrier unilaterally suggest that they're going to move to a particular really low rate. That is, to me, not exactly a well-arranged and balanced arrangement. So I don't know.

I can't recall what happened as a result of the 2008 decision that you're referring to, but I would think it would be very difficult. I mean obviously if you work out an arrangement with another carrier that's fine. But if you don't, what's the default? That's the problem. What's the default? And the default is typically I think a tariffed rate. And if people aren't going to pay the tariffed rates, then there are disputes and then we have court decisions that go through the whole thing and we take up a lot of time and we take up a lot effort and a lot of resources. So I guess these arrangements are not always worked out so well and they have produced disputes.

MS. GOLDBERG: And speaking of a default rate, on the issue of the low rate versus a bill-and-keep approach for this traffic, at what point do the accounting costs outweigh the benefits? And maybe you could speak just specifically what are the benefits of a low rate and the incentives as well? And maybe we could start with Kathy.

MS. GRILLO: I think that's a good question. A lot of carriers that have discussed the .0007 rate have raised that issue, does it cost more to bill it, frankly, than it does to move to zero.

And from our perspective, we've always been concerned about not having a positive rate just because we think that -- we're just a little bit concerned about arbitrage opportunities, just in the general structure if you had a zero. So I think that's a valid concern.

One of the things we've said is you can always move to zero eventually. Once you move to zero, it's hard to move back up to .0007. You can always go to .0007 and the Commission can decide after that whether it makes sense to keep a positive or not and to move to bill-and-keep. So that's how we've looked at it.

MS. KROENBERG: (Away from microphone.)

MS. GRILLO: That's a good question because I don't know that we do either. But it's just a concern, generally. The prior panel was really interesting because in a lot of cases you don't know where some of these arbitrage opportunities will go. I don't think anyone anticipated what happened with the ISP-bound traffic and all the problems that came out of that. So it's hard to anticipate these, which is why we think it's so important for the Commission to move quickly to a single rate. One rate that's low and uniform across the board. It just makes it easier, obviously, to avoid these sort of things.

So I don't have anything specific to point to. I mean in the wireless word carriers exchange traffic at bill-and-keep a lot. But I'm just saying from our perspective that's why we've looked at it a little bit differently.

MR. KASPER: One way you could address potentially some of those unanticipated arbitrage opportunities like backbone agreements for IP often have -- if you go out a certain balance of traffic, 3 to 1 maybe is something that's commonly cited, then you pay. So that might be one way you could go to a bill-and-keep model, but still have some protection against ways you haven't thought of for people to take advantage of the bill-and-keep system.

MS. YOUNGERS: While we think recip comp should apply in the VoIP context here, we are looking at bill-and-keep for our larger intercarrier comp proposal and that is completely dependent on whether or not traffic is in balance or not. That's exactly right. So I would echo those comments if you're looking at a bill-and-keep regime.

MR. MCGOWAN: Yes, I would simply add you would probably need the balance thing under the law I think also seeks balance in order to do bill-and-keep. So if you're not in balance, I think that is going to be a problem.

MS. GOODHEART: As we're trying to size this problem, can Windstream and others let us know how you're quantifying what percent of the traffic you're receiving as VoIP, if you have any way to determine that?

And similarly, for Verizon and others that you're carrying the VoIP traffic on your IXC as well as receiving on the ILEC side, how is the VoIP traffic growing and how has it been trending? I'd also like to get Paul's perspective on this as well, if he has one.

MR. EINHORN: We don't really know if carriers are sending us traffic as VoIP or not. We do know that there are certain carriers that have disputed traffic and said that it's VoIP and they're not going to pay us access charges on certain traffic. So that's one way we do know.

As I said in my statement, this is really a -- I'd describe it as a new phenomena. There recently have been a couple of large carriers that have been a lot more aggressive about this, so we know that that's an issue. And to me, the way I think about this is the current disputes are certainly a problem. The thing that really keeps me up at night, though, is what Paul talked about, which is the potential to pull the string on the sweater and just unravel the entire system before the Commission can do what it has set out to do in a very aggressive schedule.

So I think this is really about stability of the current system. We all agree that it's not a great system. That it needs to be fixed. But if you totally destabilize the system before you fix it that's a plan too. You've just changed that we operate and it's in a way that does not have those transitions that are so important for the goals of the Commission in terms of getting broadband out to everyone.

MS. GRILLO: Let me start on where Eric stopped on transition. We do think it's very important for the Commission just to decide this issue now. There is just incredible uncertainty in the market about this. Carriers are doing different things across the board and we think the most important thing is for the Commission just to decide this issue going forward.

I think rather than have a prolonged period after that where there is the instability that Eric talked about I think that will create momentum towards reforming the system overall. And in that context we do support and actually think it's important that the

Commission has transitions.

As Lisa said, there are a lot of moving parts when you're talking about universal service and intercarrier comp. And there are a lot of different levers that we can move to soften the landing, so to speak, when we transition from the current system we have to a single, low rate. There are a lot of things you can do with respect to universal service and other things.

So we support that. I think that's an important consideration. But for the time being, I think we need an answer to the question of VoIP and what the compensation rate should be.

To your question Rebecca about the volumes, I don't have exact numbers. I know it's relatively small right now in terms of VoIP. And you asked whether or not we were seeing that trend up, and yes. I mean I think that's where the industry is going, generally, obviously. So we will see that trend up. We will see those numbers grow year over year, which is why I think it's really important to get some clarity now. Does that answer your question?

MS. LAINE: Just to that point, I think we can agree we're on the same page in terms of a unified low rate. We agree with Verizon on that in the long term and I think we would say let's hasten that process rather than take an interim step to cause more confusion, give more incentives for people to game the system and have a separate rate in that interim period.

It's important to resolve it and keep it as simple as possible during the period that you're taking the path to a unified low rate for everything.

MR. KASPER: I guess on the point that the volume is relatively low, but growing. I mean doesn't that give us time to phase in? I mean the Commission is not talking about just adopting bill-and-keep or something like that and letting the chips fall were they may for the rural carriers.

I mean they are talking about making implicit subsidies explicit, funding it thorough USF. And if you have relatively low volume of VoIP now, that gives you a chance for you to actually get those mechanisms installed and identify specifically what the subsidies are and whether you're actually getting what you -- whether the funding is appropriate for the need, which is the problem with having things funded through intercarrier charges. You don't really know what you're getting.

MR. EINHORN: I wanted to follow up on that.

I mean that sounds good, but I think it's totally impractical and wouldn't happen. It wouldn't play out that way. the fact is that there's really no way to confirm what this traffic is when it comes in. We basically have to take the carrier's word for it. It's coming in over trunks were the traffic is often intermingled with other traffic. And this is why I put it up front in my statement, although it's not a huge problem now in terms of the disputes that we're having, they're real and they're a huge drain on our resources.

This problem can explode really quickly and I think that it probably would if the Commission were to come out and set aside a special low rate for VoIP. Suddenly, a lot of traffic that currently isn't classified as VoIP would be. And the fact that we have a lot of traffic that is VoIP today that's paying access charges suddenly all of that traffic would migrate into the bucket of the low rate. So you would have the instability suddenly that Paul talked about.

MS. GILLETT: Have there been any allegations of carriers basically saying all of our traffic is VoIP because we can't tell the difference? Has that already happened in the marketplace?

MR. EINHORN: Yes, I think increasingly that has. I don't know specifically carrier-by-carrier, but I am confident that there are some carriers that are telling us that all their traffic is VoIP. The problem is that increasingly it's bigger carriers that are claiming more of their traffic under this banner.

MS. LAINE: And it's unclear to me how on the terminating side because there is just not as much originating. But if we're taking a call from a long distance carrier and we're ultimately handing it off to a regional VoIP provider how that long distance carrier knows how it's terminating, and they're taking the position in some cases that it's all VoIP, as you mentioned.

But I'm not sure how they know on the terminating side whether it's VoIP or not. And I guess they would know from the originating side who they're picking it up from, but if it's telecommunications traffic that they're getting from the originating LEC and they're handing to the terminating LEC then how to they know to take the position that it's VoIP?

MS. GRILLO: Sharon, isn't part of the problem, though, that there isn't a clear signal from the FCC in terms of what the right rate is. So with that in place, and a system that uses factors and audits as a backstop, you may not see the result that you're talking about. Because today, in terms of what you're seeing, and frankly what we're seeing too, there is no rule. So arguably, a lot of carriers are taking the position there is no rule. So that makes it easier to do what you're talking about. So in a way, having a Commission decision and then having rules around it would help improve that situation.

MS. YOUNGERS: And I agree with Kathy. Actually, taking a step right now and interim solution would actually provide stability, not destabilized as has been suggested here.

And just to echo what's already been said, both scenarios are happening today. Carriers are treating it as -- they're sending it down local trunks, treating it as enhanced or they're treating the traffic as telecommunication service and pay switched access on it, but both scenarios are happening.

So I agree with Kathy that we need an interim proposal now to provide consistency across the board. And I actually think that provides stability. It doesn't destabilize where we are.

MS. GILLETT: Assuming there's some reasonable way to verify.

MS. YOUNGERS: Of course. Right.

MS. GILLETT: A safe harbor or some other way of verifying what is and what isn't.

MS. YOUNGERS: The factors, JIP, and then audit rates.

MS. GILLETT: It only works if there's some way, it seems to me, if --

MR. EINHORN: Just real quick, there's a data point here. The Commission just recently put out its report with lines and services and which buckets, right? And just off the top of my head I think it was--

MS. GILLETT: 21.8 percent VoIP.

MR. EINHORN: Yes, so it's a very large percentage of the traffic, and growing that is probably originating as VoIP that is paying access charges today. So I don't know why anyone would think that that traffic wouldn't suddenly fall into this other bucket. And that's a pretty big cliff to get pushed over.

MR. MAHER: This is a question that came in from the audience and I'll throw it out to any of the panelists as it relates to your proposals. But the question is, how does a particular intercarrier compensation framework, and I guess specifically for

VoIP and purposes of this panel, create incentives for the exchange of traffic on an IP basis, not only at the edge of the network but throughout the entire network?

MS. YOUNGERS: Our proposal for intercarrier comp reform, as a whole, is that the FCC when it adopts a comprehensive scheme that it include the requirement that carriers interconnected on an IP basis and it do so in a certain amount of time. We've suggested five years. And that there be incentives created to get carriers to that point, and that includes at some point if a carrier is still interconnecting on a TDM basis that that rate be different and it would be probably be higher. And that is to incent carriers to move to IP interconnection.

MS. GRILLO: I agree with that. I think it would be an incentive for companies to move to IP and help facilitate this transition to an all-IP network, which is what most of us want to see.

MS. LAINE: Yes, I mean I think that changing the regime and saying that there's something special for VoIP will actually do the opposite. I think that if the Commission were to decide that it should be treated like telecommunications traffic that you're actually indicating that there's not a preference any longer for TDM traffic and I'm not sure how you incent LEC to move their networks to IP for originating calls if they can't be assured that they're going to be compensated when those calls are terminated in IP on their network. So I think that it would actually incent carriers to move to IP to treat it as telecommunications.

And I also think that the Commission could make it clear that when carriers exchange traffic, regardless of the technology they use that they should have to accept traffic in IP format.

MR. KASPER: I'd add one specific way that I think that bill-and-keep, in particular, can help accelerate the transition to IP networks. One question that people often have about bill-and-keep is how the interconnection works, the rules for interconnection? But that's a very Telco centric view of the world. You have to build a trunk to hear, a meet me trunk between the two networks.

A lot of times for the VoIP traffic that we carry we go to Telecom carriers over the public Internet, so you eliminate the need to build trunks out to each other. So if you go to bill-and-keep it may encourage some of the -- say for instance a rural

Telco, Vonage or someone who is not anywhere close to move their traffic, convert it to IP and basically move it over the public Internet in order to interconnected with us more efficiently.

MS. GILLETT: All right, lightening round here. I've always wanted to be on the other side of this one as opposed to being in front of Congress having to do this.

(Laughter.)

MS. GILLETT: Let's go down the line. I'll start with Eric on this. What's your position on whether the compensation obligation for VoIP traffic should be prospective only or applied retroactively? A question from the audience.

MR. EINHORN: I think it applies now, so I'd say both.

(Laughter.)

MS. GRILLO: Perspective. I think there's been enough uncertainty and enough litigation. If the Commission takes a position, it should do it quickly and just make it perspective only.

MS. LAINE: And I agree with Eric. I think it applies now, so both.

MR. KASPER I would say prospectively, I agree with Kathy. There's been enough uncertainty that it would be reasonable to apply it prospectively.

MS. YOUNGERS: Prospectively, for the same reasons. There's been enough uncertainty, enough litigation, enough disputes. And in order for it to apply right now the FCC would have to have found that it's telecommunications services and they haven't found that yet, so I don't think that works and it has to be prospective.

MS. GILLETT: We're in lighting round, but I'm going to come back with a question about that later.

MR. GALLANT: Investors are entirely forward looking, so the only thing they would care about would be the prospective treatment of VoIP traffic. I mean it would be free money if the Commission were to order accrued liability to be paid to the ILEC.

MR. MCGOWAN: Retrospective would be certainly a way to increase the risk I guess to those who are taking this gamble. I mean I think prospective is the only really practical way to avoid even more disruption and chaos. So I guess maybe the flip side is quick rather than retrospective or prospective. Quick.

MS. GILLETT: There you go. Leave it to the state commission to find that middle ground. There we go.

I wanted to just go back to something you said Lisa and ask you and Julie to square it up because you're saying it's not telecommunications services and Julie you're saying its telecommunications, so can we understand why we're hearing different things?

MS. YOUNGERS: Sure. To clarify, the FCC hasn't reached a decision to date on the classification. It hasn't decided if it's telecommunication services or information services. And in fact, I think you reiterated that in your NPRM. And they would have had to have made that finding for access to apply.

It is telecommunications. That was decided in the Vonage order and other places, but obviously that's a different thing altogether.

MS. LAINE: And I think we agree. I mean the Commission has not determined whether interconnected VoIP is a telecommunication service or an information service. But apart from that, it has said interconnected VoIP traffic is telecommunications traffic, so I think that that's sufficient.

MS. GILLETT: And how does that apply in the access context?

MS. LAINE: If you think about how VoIP traffic when an ILEC hands a call to a LEC, it's generally in TDM format. It's not VoIP. And whether it's delivered ultimately to a VoIP provider and that interconnected VoIP providers provides interconnected VoIP and unclassified service to an end user that's one thing, but what the IXC hands to the LEC that ultimately gets to the end user that's served by VoIP is telecommunications. So I'm not sure that there needs to be a declaration that interconnected VoIP is a telecommunication service in order to apply access to the traffic that's exchanged between an IXC and LEC.

MS. GOODHEART: I have a question for all of the panelists. In the NPRM, we talk about working in cooperation with the states to achieve intercarrier compensation reform, what do you see as the role for the states in terms of their treatment of VoIP?

MR. EINHORN: Since we think intrastate access applies, we think they certainly have a role. And we have been involved in lawsuits in states and before state commission have decided that issue too. So we think the states have a role so long as the system is the way it is today with a bifurcated role with local and interstate traffic they have a role.

MS. GRILLO: I think that states have a role in a lot context in this debate. We think that the Commission itself has determined that VoIP is an interstate service that's subject to exclusive jurisdiction by the FCC. And in this context in term of setting the rate for VoIP that that should be done by the Commission.

MS. GILLETT: I just want to clarify. We're almost out of time on this panel, so let's make it lighting round and go down the line on this question, and it'll be our last question.

MS. LAINE: I think that the Federal Communications Commission should declare that it's subject to access charges and then the states certainly have a role on the intrastate side. And then I also think that the FCC should reaffirm what Kathy mentioned, the 2004 ruling that states shouldn't be regulating the retail interconnected VoIP service.

MR. KASPER: I would say that it's, as Kathy said as well, the FCC has decided that VoIP is interstate, more or less, in the Vonage order and they had the authority to set the rates across the board. And so I think I don't see as much of a state role in this area.

MS. YOUNGERS: I agree. The FCC has

determined that this an interstate service. I agree with what was just said, and I think the Vonage order carved out for the state public safety and consumer-type roles that could be ongoing.

MR. GALLANT: I think introducing a state role into this process, whatever the public policy benefits or the intergovernmental benefits would probably introduce more uncertainty. If there's an opportunity for states to complicate the ability of rural Telcos to collect some of these access charges, I think that would not be a welcomed development, just from the investor perspective.

MR. MCGOWAN: I don't see the states as necessarily trying to complicate it. I think the FCC has classified nomadic as interstate. It has not successfully, I don't think, classified fixed as interstate. I think that was challenged and it was deemed to be not right in the 8th Circuit, if I remember. And I think that the states do have a role in terms establishing the wholesale treatment.

I would also like to note that New York and I think a number of states have tried to be very nimble about not over asserting jurisdiction on the retail stuff, on the retail services. So I think in New York we have been very careful about trying to only assert jurisdiction that is truly needed.

MS. GILLETT: Let me thank our panelists and turn it over to Roger.

ROGER: If you can get back here by 1:25 so we can start promptly at 1:30 and stay on schedule. We have little sheets about lunch place for those of you who don't know right here at the front table. Thank you all.

(Whereupon, a lunch recess was taken.)

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A F T E R N O O N   S E S S I O N

(1:33 p.m.)

MS. GOODHEART: Good afternoon and welcome to the third and final session of the Intercarrier Compensation workshop today.

My name is Rebecca Goodheart, Associate Chief of the Wireline Compensation Bureau and I will be moderating this panel.

We head to very productive session this morning and expect a similar, lively discussion this afternoon. This afternoon's session will focus on developing a recovery mechanism as part of intercarrier compensation reform.

The NPRM makes clear that we propose to develop a predictable transition with no flash cuts. As part of ICC reform, we sought comment on how to develop a recovery mechanism to enable the industry and investor time to adjust to reduced ICC revenues.

The NPRM asked a variety of questions, including whether the FCC should focus on cost or revenue recovery, and if we focus on revenues, what revenues should be considered regulated and non-regulated, net revenues versus gross revenues and how the FCC should look to reasonable end user charges and finally developing a criteria for access to the Universal Service Fund for areas that are uneconomic to serve absent support. We also asked data to help size and develop the recovery mechanism.

We have an excellent panel ready to dig into these issues as well as a distinguished team of questioners. This panel will be 90 minutes. I will first introduce the panelists and my colleagues and then each panelists will have three minute to summarize his or her positions, followed by questions from the panel, the audience, both online and in person.

Turning to our panel, we have John Rose, President of OPASTCO, Ken Mason, Vice President of Government and Regulatory Affairs for Frontier, Bob Quinn, Senior Vice President, Federal Regulatory and Chief Privacy Officer for AT&T Services, Charles McKee, Vice President, Federal and State Regulatory for Sprint and Nextel, David Bergmann, Assistant Consumers Counsel Chair, NASUCA Telecommunications Committee, and Frank Louthan, Managing Director, Raymond James.

We are also honored to have Iowa Board member Krista Tanner as well as Peter McGowan, General Counsel for the New York State Department of Public Service, who have agreed to ask questions on this panel.

Joining me as questioners, Victoria Goldberg, who is an attorney advise in the Wireline Bureau's Pricing Policy Division, John Baker, our chief economist, Bill Sharkey, senior economist and OSP. Next to him is Dan Ball, attorney advisor in the Wireline Competition Bureau, and Kevin King, who is a telecommunications broadband analyst.

And with that, I'll turn it over to John.

MR. ROSE: Thank you for inviting OPASTCO. OPASTCO has 470 small rate-of-return regulated companies across the country. Our companies are committed to achieving universal broadband availability and adoption. The National Broadband Plan recognizes the need to create the right incentives and one of those incentives is intercarrier reform and having a recovery mechanism.

This is a very important point to us and there's one message that I want to leave with you today is that to be beneficial to rural consumers it's essential that there's a sufficient recovery mechanism to provide the RLECs a transition.

It is important to remember that RLECs rely on access charges for 30 percent of their revenues and USF for another 40 percent, which equals 70 percent. The lack of an adequate recovery mechanism will necessitate significant rate hikes for both basic and advanced services and this is to repay loans.

Beginning to come up with a plan is that we recommend as a first step the Commission enable RLECs at the option of the state commission, and Chairman Genachowski mentioned of this this morning, is to lower intrastate originating and terminating switch to access rates to interstate level. And this would be with a benchmark rate of $25 or around. That would include the local rate and interstate and intrastate SLCS, contributions by state USF.

In the first year, RLECs would be permitted to recovery the revenue loss after the voice rate benchmark has either been charged or imputed. In subsequent years, as the switched access revenue goes down, so would the recovery mechanism. We believe this is a balanced approach and would immediately eliminate a major of rate arbitrage and could help contain the fund.

The adoption of a benchmark would be fair to earlier adopter states. The total estimated revenue loss to RLECs from reduced of the intrastate rates to interstate levels would be around 300 million. With the adoption of the benchmark would put it probably under 200 million. And then if we adopted some phantom traffic reforms as well as VoIP access that would make it even lower.

And we think that it's a major step to fix phantom traffic, to address VoIP, to create a restructuring mechanism, lower intrastate rates down, and once these steps are taken I think we could go look into further steps and have a reasonable transition. Thank you.

MR. MASON: Good afternoon. I would like to thank Chairman Genachowski, the FCC Commissioners, and the Commission staff or hosting today's workshop and for providing Frontier an opportunity to present its views on the important topics of intercarrier compensation and universal service reform.

Frontier supports the steps the Commission is taking in evaluating reform to both intercarrier compensation and the Universal Service Fund. Currently, Frontier receives approximately 10 percent of its revenues from these sources.

Not surprisingly, these two sources of revenues are critical elements supporting Frontier's aggressive deployment of broadband to our rural markets, markets where we will never have the scale, scope, or a customer base comparable to what exists in more urban parts of the country.

Given the integrated nature of this support, it is critical to reform ICC and USF in lock step as action on one can have direct impact on the other. We recognize and accept that there will be an impact on the way recover for ongoing investment in our rural markets going forward, but we also point out that these revenues enable mid-size ILECs like Frontier to meet the Commission's challenge of deploying broadband to rural America.

Last summer, as part of our acquisition of 4.8 million access lines from Verizon, Frontier made aggressive commitments to deploy broadband and improve service. We were able to make that capital investment commitment, in part, because of the revenues that we received from universal service and intercarrier compensation.

The primary theme you will hear form Frontier on reform is transition, whether it is the phase down of ICC rates or the shift of the Universal Service Fund into a more explicit broadband fund, it is critical that these transitions occur in a way that are gradual and predictable in order to provide an appropriate guide path for Frontier and others. Companies must be given the ability to adjust for these changes in their business to ensure that ongoing investment in broadband in rural and high-cost areas can continue.

Transition must also be the central theme of any discussion of access recovery and should affect the way the Commission balances its goals of modernizing ICC and USF for broadband while controlling the size of the Universal Service Fund. In fact, an appropriate transition is the key to making sure these goals aren't in conflict. Any transition that is done too quickly will place the burden on the companies that currently collect ICC and their rural end users.

Recovery of ICC revenues from end users rates needs to be measured and limited as is any use of the Universal Service Fund. Frontier does not expect access recovery to provide dollar-for-dollar replacement and acknowledges that ICC is a revenue stream that is currently declining. However, it does remain an important source of revenue and cashflow. Cashflow that provides Frontier to expand broadband availability to large areas of rural America.

Moving to a proposed ICC end state without the opportunity to replace or at least have the opportunity to replace substantial amounts of these foregone revenues for a period time will directly impact Frontier's ability to continue to invest. Frontier agrees the USF is currently under pressure, both in size and in terms of the end user contribution percentage.

However, to ensure that mid-size companies and other rural LECs, especially those who have made explicit commitments to expand broadband continue to have adequate cashflows to meet those commitments the FCC will need to examine whether additional access replacement funding will be required from the Universal Service Fund. Frontier believes that answer is yes, but this amount can and should be controlled by the speed of the access rate shift.

The best approach is a step down and phased out fund over time. The critical period will be the steps when moving from intrastate access rates down to interstate access rates. We envision the fund that would allow for recover of a percentage of those displaced revenues after a limited end user increase with that recovery declining over a fixed period.

The amount of the transition fund required will be dependent on the overall transition. The longer the transition period the smaller the transition fund and the greater the likelihood that companies like Frontier can continue to confidently invest in rural broadband deployment, therefore meting both of the Commission's goals for reform.

Again, thank you for allowing Frontier to be a part of today's panel.

MR. QUINN: Bob Quinn with AT&T.

The recovery mechanism should be designed in the context and to promote the overall vision from universal service reform. We have to in this country move our universal service support mechanism and the intercarrier compensation regimes from supporting voice service to support of broadband infrastructure in this country.

And I think we have to recognize the point that John made that today the access charge regime comprises a significant portion of revenues that are received by rural and mid-sized carriers in this country. As part of that migration, I think there are going to be two critical points that are going to serve really as the reality that we're going to have to deal with.

Point one is that we're not going to replicate the existing access charge regime in this new world where the support mechanism is going to be designed to support broadband infrastructure. The second point is that reasonably comparable prices for broadband services in high-cost areas are going to be higher than the price that we pay today for basic local exchange services. We're not going to have, in my view, a seven or an eight dollar local service rate in the broadband environment, and we have to recognize that.

We have two principles for the recovery mechanism that are very important. The first is fiscal responsibility and what we mean by that is that the recovery mechanism should not create a windfall. We should utilize benchmark rates along with SLC increases and provide the providers flexibility to ensure that end users in high-cost areas who have historically enjoyed very low rates bear a fair share of the burden of the broadband infrastructure in their areas.

The recovery mechanism should also be sized to reflect reductions in lines and minutes, where appropriate, to ensure that service providers not recover more than they would have in the absence of intercarrier compensation reform.

The second principle that's very important is that access shift should be transitional. It should help us bridge the transition as we go from a voice-supported environment to a broadband-supported environment. Ultimately, when that transition is complete, the funds should go away and the Commission should look into establishing the benchmark rates that I think are going to have to play a big part of this. They should also look at raising those rates over the course of the transition period.

And with that I'm out of time, so we'll just go to questions when it's time.

MR. MCKEE: Thanks. This is Charles McKee with Sprint. I appreciate the time today.

From Sprint's perspective, the goal of intercarrier compensation reform needs to be creating an environment in which competitors can flourish and moving away from a system that has been designed primarily to funnel money away from new entrance and competitors to fund the incumbent local exchange carriers.

In doing that, we understand that there is going to be areas in which there is high costs and it's going to need to be addressed. But to the greatest extent possible we should be moving to a system in which carriers recover their costs from their own consumers. In doing that, businesses will have to recognize that technology and consumer expectations change and business plans have to change to accommodate those changes in technology and expectation.

It appears that the LECs, at least to date, have begun to address that. And in fact, the LECs have been aware for many years that these changes have been coming. Indeed, we've been waiting 15 years for these changes to be implemented and it's no surprise that we're going to be moving to a new system. There are new revenue streams for LEC. There are greater efficiencies in the current LEC networks, all of which should reduce the need for a revenue replacement mechanism. Nonetheless, we recognize that one may be necessary.

It needs to be limited in size, however, and in duration, and should be based upon actual need and not simply a guarantee of a continued revenue stream at current levels. A revenue stream alone is not an indication of need. Accordingly, we're going to have to look at actual cost to determine the need for an access replacement mechanism.

Ongoing subsidies have a cost to the marketplace. The reduce the possibility of competition. They prolong market distortions and they defer the benefits of ICC reform to consumers. Accordingly, we feel it's important that the

Commission move as quickly as possible to a system that does not subsidize competitors, but rather looks to the end users for its basic recovery system.

That's all I have. Thanks.

MR. BERGMANN: Good afternoon. I'll repeat what the other panelists have said all day is thank you very much to the Commission for having us here on this panel. I especially want to thank Commissioner McDowell this morning who talked about how important the interest of consumers are in this whole process. And I would note that apparently I'm the only representative of consumers on any of the panels today.

And there's a lot of talk about building consensus and it appears that there may be some consensus among the industry. But does it make me a luddite to point some of these fundamental questions out? Does it make me a heretic not to have drunk the kool aid? I don't think so. But on behalf of those who pay for all of this and those who are supposed to benefit, I feel it's my responsibility, representing NASUCA to continue to ask these questions.

And the questions include whether the reductions in intercarrier compensation are necessary and the question of whether recovery is necessary?

We're going to continue to point these fundamental questions out and point out the law where it may be inconvenient. And to quote that great savant Yogi Berra, this to us sometimes seems like it's deja vu of deja vu of deja vu all over again.

From the customer perspective, you can and should fix the traffic pumping and the phantom traffic issues, and you should also require intercarrier compensation for VoIP traffic. Those will have an impact on consumers, but eventually as they work themselves out. But the recovery mechanism, obviously, will have a direct impact on consumers.

These proposed increases to the subscriber line charge, first, not only go away from the original purpose of the SLC, but also burden low users. And of course, it's likely to drive more customers from wireline to wireless, which some of the members of this panel might be happy about. And changes in the USF, of course, spread that burden more widely.

But in the end, what you're talking about is reducing these revenues, and are we talking about reducing these revenues because the charges are going to be reduced below costs in order to create a subsidy in the true Faulhaber sense of the word? But if you put intercarrier compensation at its economic cost that means that the revenues should be adequate.

In the end, flowing these dollars through the Universal Service Fund without examining the fundamentals of the statutory purpose of universal service is asking for the customers of other companies in other states to support the revenues of the carriers who are having their access revenues reduced and we're going to continue to ask questions about that. Thank you.

MR. LOUTHAN: Good afternoon. My name is Frank Louthan and I'm with Raymond James. I'm an equity research analyst here. So just a quick disclosure up front. None of the companies we talked about today do not earn shares of any of the stocks. Raymond James may have some business relationships with some of these company. If you have any questions about that, you can feel free to see me later.

But with that said, I'm sort of independent here. I cover the rural LECs. I cover AT&T and Verizon, Comcast, Time Warner Cable, the CLECs data centers. I pretty much cover this whole space. And when I look at this my job is try and tell investors what I think about the space and where is the best place to invest, which from a public policy standpoint is something that it should be paid attention to because ultimately it's this investment in these networks that provides these services and without the investors and without the cashflow there, then you won't see that over time. And that ultimately becomes a problem.

I've heard a lot today. A lot of comments about the revenue side of this and how revenue potentially looks at it. And when we look at the valuation from an investor standpoint, we look at the free cashflow, which basically is a measure of your revenues less your cost and reinvestment in the business to determine what's left for the shareholders. And when you look at that, the intercarrier compensation, whichever flavor it is.

And it's in my opinion and I think Wall Street's opinion universal service access to the intercarrier comp is pretty much all the same. When you get that there's a revenue aspect and a cost aspect as well, and the real impact is the net impact. Because if you were to take away that revenue, a substantial amount of cost would go away as well. And that's something that we try to educate our investors on quite a bit because some investors would look at some companies and say if all this went to zero, oh no, there would be no free cashflow. There would be no more company. It's not necessarily the case, although it is clearly important.

And the other thing that I think is important that has come also today that I think from a public policy standpoint the Commission and others need to look at who's ox is going to get gored here? And everyone is going to have to end up paying some higher costs, including the end users.

And there's not really been a market rate for Telecom services, the customers have never paid and they don't understand that because the whole intercarrier compensation system has really distorted the economics of the business. And that's a public policy decision that I think is something that the Commission and the states are going to have to deal with.

The important thing is this really should be a very long transition and to very slowly and predictably put this in place because these businesses can take time to transition and with that you have time to educate the customers, but I think that's an important thing that I haven't discussed as much in the past. And I'll turn it over to Rebekah.

MS. GOODHEART: Thank you everyone. I'll start it off. Both David and Frank on the consumers and previous intercarrier reform benefitted consumers through lower long distance rates and more competition. Today, with bundled service offerings, how should we evaluate the potential benefits to consumers?

MR. BERGMANN: I guess the fundamental question is the question that you just asked and lowering the long distance rates when so many customers now have bundled packages is probably not going to have that great an impact on the cost that customers pay for their long distance calling.

But on the other hand, loading the costs onto local rates by increasing the SLC or by other rate increases is not going to help consumers. So I' not sure there's been a definitive benefit to customers shown in any of this.

MR. LOUTHAN: In general, and especially when you go back to the calls orders and the MAG plan and so forth, there were several step downs in rates and they weren't necessarily always passed on to consumers, at least after a certain point they weren't. But I think your questioning about a bundling is really important because that's generally how most customers are buying services these days. And you can talk about adding the SLC and so forth.

These are all regulatory terms that the customer doesn't really think about. They know how much of a check they write every month and that ends up being what's really important.

And if you really want to make a proceeding correct, you need to look further down the road and where we're going. We're going to more of a broadband world and eventually both on the wireless side and the wireline side, I think you'll see the industry charging by the amount of bandwidth you're using. So a lot of this over time doesn't become relevant. And there have been sort of the law of unintended consequences that have been talked about earlier today in other panels, such as the access pumping and so forth where someone finds a way to get around it.

I think it's very important as the Commission takes these steps to reform these things that they make sure that you look at where the world is going and you don't put a policy in place that becomes outdated very quickly.

MS. GOODHEART: All of you mentioned sufficient transition time. It would be helpful if we could go down the road to see what you suggest as a transition. I'm wondering if a long transition in Wall Street terms as maybe different than the regulatory terms? Can we start with you, John?

MR. ROSE: We think in terms of maybe a five-year transition. But one of our issues is we rely much more on intercarrier compensation than other carriers. Frontier said 10 percent. We're up at 30 percent, so we do need a significant period of transition to adjust to this.

MS. GOODHEART: When you're saying five years, that's intra to inter or for the entire transition?

MR. ROSE: I would think that would be you go to intra to inter first, then five years on top of that.

MS. GOODHEART: Ken?

MR. MASON: We would be looking at about a four-year transition of the first step and then some period of time to go down to whatever the ultimate end rate would be. John's five years sounds good to me.

MR. QUINN: I'm going to give you some numbers. In 2006, when we finished the acquisition of Bell South, the combined company on a pro forma basis had over 37 million residential access lines.

We just issued our annual report for year end 2010, four years later. We have 22.5 million residential access lines. Frank made the point that when revenues go away, costs go away. That's not how it works, right, not in our environment, not the way that the regulatory environment works.

Back in 2008, when we were in front of this Commission, we filed a number of dials ex partes to talk about the access shift and I think we sized that access shift at about 4 to $3 billion, given the fact that we were only talking about the terminating side of that issue. And in some of the preliminary analysis that we're doing today, we're looking out three years. So there's a five-year time frame. And the size of that access shift looks like it's going to be just over $2 billion total.

So when we talk about transitions, we're in a free fall. And I don't think anybody can plan on having the kind of transition that's going to provide the absolute certainty because we're already way through this transition. And if we don't do something very quickly, we're going to get to a point where there's not going to be a point to do anything at all because the numbers are in free fall.

So I would argue for you that our transition ought to be as short as we can possibly make it because technology and the market is transitioning this stuff today and it's not going to stop.

MR. MCKEE: So I joked when Bob sat down that they must have seated us next to each other in the hopes of conflict, and I find myself in the awkward position of almost immediately agreeing with Bob on something.

(Laughter.)

MR. QUINN: That is awkward.

MR. MCKEE: That is awkward, almost embarrassing.

(Laughter.)

MR. MCKEE: As I said earlier, and I think we need to recognize this, so the comment was made about people moving to wireless. That's right. People are moving to wireless. They're not being forced to move to wireless. Wireless rates are not being subsidized. People are choosing to move to wireless. They are choosing to leave their land line services and they're choosing a different service.

Technology has effectively moved to a position where that's where consumers want to choose to use their services and that's what they're buying. So that's right. We are moving, and it's not just wireless, of course. It's also broadband. People are moving onto the Net and they're using the Net as their replacement for voice transmission. That's a choice that's occurring today and has bee happening very rapidly.

As Bob points out, we have 280 million wireless connections. I keep losing track of where the number is on the land line, but it's been dropping dramatically and continues to do so. But the point being that the government is not going to be able to somehow stop that tidal wave of change. And the government is not going to be able to somehow slow that down and say, well, that's not where we want consumers to go.

So my point is I agree with Bob. We need to do it as quickly as possible. And frankly, we just need to move to the point where we're actually trying to live in a competitive environment as much as we can, recognizing that there is going to be some need for other cost recovery.

MR. BERGMANN: I guess from the customer's perspective, since we are likely to be impacted by whatever recovery mechanism is arrived at, I think we would prefer a longer perspective, a longer transition. And also, I think that the transition needs to be long enough so that this will work its way through the courts as inevitably will so before the transition is over we will know whether what the

Commission did was legal or not. And maybe we'll never know that.

I would also point out one thing. An interesting thing about the use of wireless versus wireline. If you take the number of folks who are unemployed and under employed in this economy, I think the latest statistic on that is about 28 or 29 percent, which is coincidentally right around the number of folks who are wireless only. I'm not sure there's a causal connection, but it something that needs to be looked at.

MR. LOUTHAN: I would argue from the investor standpoint that a rapid transition would not be a good thing from an investor standpoint or a public policy standpoint. The time frame is not really as important. Investor just want more certainty. They want to know what the rules are. Is it going to be heavily regulated or not very heavily regulated? Once you make the decision, the investors can make their valuations in investments appropriately. So as long as there is a set plan and the time frame is known that would be much better for investors.

If it happens very quickly, you'll see investment dollars leave the space. That threatens capital in the space, threatens reinvestment, and threatens more broadband build out and other things. Once there is more certainty, I would argue that valuations, and especially for rural LECs are depressed because of the uncertainty about what's going to happen with intercarrier compensation and USF, and ultimately what sort of transitions might happen. There are competitive threats as well, but that's a big factor there.

And if that issue were resolved, I think you could see valuations rise and you could see more investment in the space, which from a public policy standpoint is probably a good thing as well.

MS. GOODHEART: Can you just clarify the term when you talk about rural LECs you're talking about?

MR. LOUTHAN: I'm generally thinking of the public companies as was mentioned earlier this morning, but even some of this is not an RBOC, so Windstream. I guess Century would now be in the RBOC category -- Windstream, Telco, Consolidated Communications, Alaska Communications -- those are the companies.

MR. ROSE: As a follow up, our members realize that broadband is the future. We realize that voice-only PSTN and land lines are on the decline. The transition for us enables us to make that change and it doesn't disrupt the customer. We are building and working as hard as we can to get broadband. And the comparisons that both AT&T and Sprint made were more or less PSTN to wireless.

Our look at this is we're transitioning from voice-only land lines to highspeed Internet as fast as we can because we know that's the business of the future.

MR. BAKER: Good afternoon. I'd like to push on what revenues means when we're talking about developing a recovery mechanism and ask for some views on which revenues should be considered? We could consider just regulated revenues. We might add some or all unregulated revenues. We could consider revenues from affiliates as well. And just to sharpen it a little bit, in your earlier remarks a few moments ago I think I heard both Mr. Bergmann and Mr. Louthan say they think about the issues on the table here based on the financial situation of the enterprise as a whole. So does that push us to thinking about all revenues in developing a recovery mechanism, or is there a case for limiting the universe of revenues that we would consider? And it's really for all of you who would like to answer.

MR. ROSE: My answer would be I think we should look at regulated revenues for intercarrier compensation, both state and intrastate.

As far as unregulated revenues, our guys in the video since we pay significantly more for content than some of the larger MSOs, I mean our video stuff is barely making it and we have I would say maybe 40 or 50 percent of our companies are losing money on video. So if you're going to have that type of revenues, you need the cost to go with it or have a net revenue because I mean we're struggling with video.

MR. MASON: And I would say Frontier's opinion is very much the same. When we look at replacement, we are looking at the switched access or the revenues related to intercarrier compensation, both at the state and federal level. And that's really how when we look at it internally even how we're sizing what we see as the potential risk and determining how we think we would need to move through this, whether it's replacing through a fund or replacing through an end user or having to transition long enough that we can actually limit how much of that we need to do.

MR. BAKER: I was just referring to the switched to access revenues. That's all we were trying to size back in 2008 was what is the implicit subsidy that's built into switched access and where is that going. So that's what were my references were, were simply to the regulated intercarrier revenues.

MR. MCKEE: With respect to revenues, it seems to be the question of what's the goal of the transition. Simply making carriers whole would seem to undermine the idea of a reform. And the question is what revenues need to be replaced. There's an assumption I think that all revenues must be replaced because they're somehow needed. I think there needs to be a demonstration of need. So our starting point is not to look at revenues. No surprise. Our starting point is to look what is the cost.

But certainly, if you're going to look at revenues, you need to look at all the revenues that are being recovered off of the plan that's being subsidized. So if you have a situation where you have a benchmark of $20 and in a high-cost area the LEC says that my cost of that loop is $27, but they're selling services and getting ARPU off of that loop of 120 by selling additional services on the same loop.

Does it make sense then to say, but we need to pay then an additional $7? There needs to be rationality to what revenue means, actual need for that revenue, and then a structure for how that's going to be addressed.

MR. BERGMANN: In this instance, I agree with Charles. I think to use the metaphor that was current a couple of years ago, the question is what are the spigots out of which the dollars flow. I think it was AT&T that talked about dials. I hope I'm remembering this right. There were only three dials in their analysis. And of course, there are far more than that.

So if you were talking about replacing revenues, you do need to consider all the sources of revenue that the company is making. And if a small company is losing its shirt on the video, then they won't have the revenues to be considered and they will still need support.

MR. LOUTHAN: I would agree. This gets back to my earlier comment. We've got all these regulatory divisions on the customer's bill and all of these sort of arbitrary things that the customers don't necessarily understand. And then if you look at what is all this network providing, and I listen to hearings and I see things. And the elephant always in the room is you're talking about where we're going to bring support to support broadband and the elephant how do you think this stuff was built? I mean how did the SL get built originally? If these companies weren't profitable because of the revenue recovery, they never would have been able to build the SL to begin with.

And now we have, from what I hear from the Administration, is they have a policy of pushing more broadband out to rural areas. And here you have companies that demonstrated for a hundred years in some cases that they want to serve these customers. You really need to look at in aggregate. And I think that's just important because moving to support broadband and support all the services that these networks are providing and that the customers want that's really the only way to look at it.

Now I think the danger and the concern to some in the industry they think that would get us down to regulating even more parts of the industry. I think the regulatory bodies need to look at this and say what services are you providing? Can we just let these companies operate, not be so concerned about whether -- let them make some money and then they can reinvest it and provide even more services because ultimately you do have competition in certain parts of your network. And if you don't reinvest and add more services, then you'll be in trouble, such as the video side of things that they were talking about from OPASTCO.

MR. SHARKEY: Yes. Hello. I have a question that pertains to the end state or the long-term reform as it might apply to rate of return carriers. So just assuming that in a future order the Commission adopts some of the proposals in the NPRM that set interstate and possibly intrastate access prices on a path to cost-based or perhaps bill-and-keep, then clearly they will no longer be determined according to rate of return principles.

So I have two questions. First, to what extent after the transition is complete will there be a need for a recovery mechanism of presumably a cost-based recovery mechanism? And second, if so, to what extent or how can that be determined, or should it be determined by principles of incentive regulation, or if not, what else might apply. And I guess John should address this first, but others are, of course, welcome.

MR. ROSE: The end game to me would be pretty much an all broadband network. And we think the Commission is looking at the Universal Service Fund, the CAF and everything to transition to that world. And we plan on we would be rate-of-return regulated. We would need the CAF support to get the broadband and to keep up with the speeds that we know are going to be necessary to compete in this world.

So I mean we think it's going to transition to an all broadband world. The restructuring mechanism for intercarrier comp. I think over time would go away, but we would hope that we have enough universal service funds so that we can provide broadband at the same rates and offer the same services and speeds as the rest of the country per the '96 act. And we understand that rate of return is a way of doing that and we prefer that way over some price CAP mechanism.

MS. GOODHEART: And John, I think Bill was talking about just the switched access revenue requirement, not sort of the common line or special access because if you don't have it in your carrier rates how do you have rate of return?

MR. ROSE: I mean that would transition down to zero then if no rate of return. I mean I'm assuming that at the end game we're talking about that we wouldn't have a PSTN, that it would be all broadband and we wouldn't have a rate for switched access and we wouldn't have any costs either.

MR. SHARKEY: But the small carriers would still be made whole in some sense in your view by rate of return?

MR. ROSE: Right. And we would hope that the future USF mechanism would be good enough that we can actually provide the broadband at the speeds our customers want and at the prices they can pay.

MR. SHARKEY: Other comments?

MR. QUINN: I agree with John that the end state here is going to be a broadband world. And I think that's what the Commission's goal is with the National Broadband Plan. And I think you make the assumption that there is no intercarrier compensation in that world, there is no access charge regime that operates in that world then that perspective, all of that money goes.

And then I think you've got to look at what are the revenue streams that are going to be available to the entity that's providing broadband service. And I think today John gave a good breakdown of it. It's 30 percent form the end user, 40 percent from universal service, 30 percent from intercarrier compensation in order to be able to provide the cost of providing voice services.

In a broadband world, I think the two sources of funding are going to be via the end users and via some contribution from universal service where broadband would not exist but for the use of universal service dollars to be able to provide broadband services.

I don't know what that world looks like. If it turns out to be rate of return for some carriers in that environment, it's not going to look like rate of return today. But I think what you're going to be trying to do is you're going to be trying to establish a regime whereby the end user is contributing a fair portion of the cost of providing that service and the balance comes from the Universal Service Fund. And by focusing on efficient technologies, I think you're going to be able to provide some form of discipline to that at the end of the day so that the consumers are contributing and we're going to try and be as efficient as we can with the limited universal service dollars that we have to be able to provide services on comparably reasonable rates throughout the country and speeds throughout the country, as John pointed out.

MR. SHARKEY: Thank you.

MR. LOUTHAN: I would throw one more thing in there. I've read a lot recently about rate of return regulations seemed to be vilified because it's come to people's attention that it's not very efficient. But when we look at that this, there's one factor here that's really changed. Rate of return in my simple analysis was a business arrangement between regulators and the companies.

We'll give a monopoly, but in exchange we're going to limit how much money you make, and we're going to require you to bill to everybody. And so you get to bill to everybody and it made sense. Very good plan. But now you've brought competition into the mix and that wasn't the case before. And so I think moving to an incentive-based regulation is probably something that's palatable, but there have to be some offsets for the competition that's there, whether you're going to continue to require the carrier of last resort obligations and so forth if you're moving to a more incentive regulation, more actual cost-based and then more actual cost-based revenue that you're charging the end user.

I think that's one aspect. If you're going to start messing around with rate of return, the competition factor has to be considered.

MR. BERGMANN: Let me just add from the

state perspective, of course. I think the references to "rate-of-return" regulation have larger have been on the interstate side because on the state level, of course, very few carriers remain regulated under rate-of-return regulation.

In my state of Ohio, by law that was passed last year, nobody is under rate-of-return regulations, so they're entitled to set all but basic service rates at any level they want and they're entitled to earn as much as they want. And in fact, what rate-of-return regulation from the customer's perspective was a guarantee of a minimum level of revenue. There have very, very seldom been any high-end adjustments on the state level for rate-of-return carriers.

MR. QUINN: David and Frank make an interesting point. And I think really we have to put their two thoughts together.

In the old days in a rate-of-return environment, a hundred percent of the customers or virtually a hundred percent -- I think we achieved north of 99 percent penetration on voice services subscribed to one carrier service.

When I look out at the world tomorrow, I'm going to tell you that a third of the customers are going to chose a wireless only option. And I know that there are a whole lot of people out there who tell that wireless isn't the be all/end all. You can't do what you can do on a wireline. I heard that in the Net neutrality debates at this Commission, but that's not the reality. Wireless is going to be a very viable service and a third of the customers are going to choose a wireless only option.

And if there's a cable company present, a third of the customers will chose the cable competitor and a third of the customers may chose an incumbent provider of wireline broadband services.

Rate-of-return regulations had two components. And while David points out on the rate side and the return side, all of those regulatory obligations are gone, but the Kohler obligations and all of the legacy regulatory responsibilities are there. So in that environment I described where I've got three customers and each choose a different broadband delivery mechanism for them that local incumbent, if something is not done still has to maintain all three loop infrastructures, even though two of those customers are never going to be there.

When I think John talks about rate of return, I think that's one of the critical aspects that underlies his analysis of why it's so important.

And I think to Frank's point, it also underscores how difficult that concept is going to be address. We have to deal with the underlying regulatory environment that's there or none of this is going to work.

MR. MCKEE: The issue becomes is there a reason why you continue to subsidize when you've got two alternative providers who are, in fact, providing service to those customers. So is the question then going to be you need to look more carefully on how those dollars are being spent and whether or not they, in fact, are being spent wisely.

I think, though, the point that was made earlier is an important one. And that is, the reality is rate of return is a very small portion of what the total universe of lines is. I think Verizon, AT&T hold roughly 77 percent of all ILEC lines. And if you put in the new CenturyLink that pushes up to 90 percent of ILEC lines. So for those smaller carriers it may be reasonable to have a different transition path. Maybe that's a more difficult issue to resolve, but I still think we need to address the bulk of the stuff now and those are really the big carriers.

MR. MASON: I guess I'd like to answer the question a little bit differently and probably a little bit self-serving.

Frontier is predominately a price-CAP carrier, yet it finds itself in a unique position, particularly with some of the concepts laid out in the NPRM that companies that have made explicit commitments as part of transactions to deploy broadband are not eligible for the CAF until they meet those commitments.

And so a new fund that's established for broadband would not be available at potentially the same time we would have revenues moving very rapidly, if Charles has his way, would obviously make it much more challenging for us to meet those commitments than we contemplated when they were agreed to.

MS. GOODHEART: I mean in terms of the eligibility you might be eligible for the areas that you committed, but I think you would be eligible for other areas to compete.

MR. MASON: And if that's the interpretation, I guess that's fine. But the way we had read it was we needed to meet those commitments first.

MS. GILLETT: No, could I clarify?

MR. MASON: Sure.

MS. GILLETT: What we were trying to say was we were not going to use universal service going forward to pay for commitments that were made prior to the reforms. So whatever you committed to you need to do, but if you're going to get universal services you've got to go beyond.

MR. MASON: I think the result is the same result as what I'm saying.

MR. GILLETT: It doesn't mean you have to complete everything before you could consider getting CAF.

MR. MASON: But the result is still the same result that I'm speaking to, which is we can only use CAF then let's just say for the last 15 percent of an area that we hadn't committed to. And yet, potentially have our revenues and cashflows dramatically changed to try to meet the jump from X percent to the 85 percent over that. And that's where on a transitionary basis we think some access shift becomes critical for us. And so it's a little different spin than a rate of return spin, but one we think is important.

MR. KING: My question was picking back up on the issue of revenue replacement for those carriers that were advocating for switched access or regulated revenue replacement. I'd like to get a response to

Frank's original point that was at the very least shouldn't you factor in your intercarrier expenses that you pay to other carriers as well operational savings that reform offers in terms of lower billing, collections, and litigation expense in terms of what you need to be measured on for the loss?

MR. MASON: From Frontier's perspective, I think, conceptually, looking at what we're paying for wholesale long distance traffic and the savings that potentially can come along from that, I don't think that's unreasonable. Is there a guarantee from the IXCs that we're going to see that pass through on the wholesale side? I think the point being is there no guarantee in the contracts that we would have. We would have to back and renegotiate those to see those things.

MR. LOUTHAN But it doesn't have to do with what the IXCs are going to say because I never see that, but there is a certain line in your GNA line for all the carriers that you're paying for access. When you call interstate, you're getting four cents a minute for originating, or whatever it is.

MR. MASON: But in a lot of cases we're paying a rate to the wholesale provider and it may be a combined originating transport terminating rate that's a fixed rate. So for that state, this your rate. For this state, this is your rate.

MR. LOUTHAN: But if you unify all the rates or if they go down, there would be some element of your cost that would also go down at the same time. And the net affect of that it may be large. It may not be. I would argue that you're probably a net receiver of access on the margin. John's customers are probably very large net receivers. AT&T and Sprint are net payers.

MR. MASON: And you're right. All I was trying to say is there's a piece of that savings that we would have to negotiate before we saw the savings, that it's not a guaranteed pass through.

MR. KING: But that's a timing issue, right?

MR. MASON: Yes.

MR. KING: A lot of your contracts probably have it written in there that there is a pass through of cost saving that your IXCs realize on access. If not, when you have new IXCs come and compete for your business once the rates are low at better rates.

MR. MASON: Very possible. Yes.

MR. QUINN: But here's the reality. And the reality is that access charges get paid in the long distance market, right? Long distance carriers are paying the access charges. So when Sprint's access charges go down and that cost goes down, and my access charges go down as an LD provider that's going do drive the rates of long distances services down. It just is because that's the competitive market. But the access revenues are coming to the long distance services side of the industry. They're coming to support the local infrastructure. So you're talking about two completely different revenue streams. You're not replacing the revenues on the local side to support the local infrastructure.

What's going to happen when you take the access charges out of LD rates they're going to go down further, not a thriving business, by the way, right? I mean when we were talking about access with David ten years ago little bit different business than it currently is today. But what you're talking about now is you're talking about saying access charges come down. The competitive model of long distance, and believe me that's very, very competitive.

My kids don't use long distance. They use Skype, right? They're on Skype video. They're on Skype long distance. So that's a very, very competitive market and it's a very competitive model. You take cost out of that service segment and the rates there are going to go down, but that's not going to replace the revenue on the local infrastructure side of the house. It just isn't. And you're just taking money out of the system from the local part of the house that needs the support to support the local infrastructure.

MR. ROSE: To address your issues, one of the reasons we said we have a benchmark right is to make sure we get up to that amount from our customer. And so that would be a net offset. The other thing is that we think that to the extent of fixing phantom traffic and also including VoIP as a telecom service we think that might increase some, and we fully expect that would net out against what's in the restructure mechanism too.

We understand the idea is if you fix these things that that restructuring mechanism would be lower and have less pressure on the Universal Service Fund. So we were looking at a net amount.

MS. GOODHEART: So I actually have two questions. The first question comes from one of our web participants, and the second question has several parts, so feel free to take notes.

The first question from the web participant was, with today's integrated local and long distance companies and with competition from wireless and VoIP, why have a SLC at all? And the second question is, in the event that SLCs should pay a role in the recovery of reduced ICC rates, what are the relative merits of using a level increase in SLC rates, using SLC rate caps that are tailored to some level of network usage like a variable SLC and how would that work, given the popularity of bundled offerings or some sort of restructuring of the SLCs in some other manner?

MR. QUINN: Many CLECs don't have SLCs, right? Many CLECs and wireless companies don't have SLCs, but they don't have their local rates regulated. I think if we removed the regulation and you provide a certain amount of flexibility I really don't care what bucket it falls into, but you have to provide the flexibility to the carrier to be able to recover the lost revenue or the cost of providing the service.

MS. GOODHEART: Bob, in some states the local rates aren't rate regulated, so what do you suggest happen in those states because there are some states, and I think Iowa is one, were the local rates aren't regulated by the state?

MR. QUINN: I think to be fair, and I don't provide service in Iowa, right? But to be fair, if the local rates aren't regulated as long as you have the flexibility to be able to recovery it that's all you can as for as a carrier. I mean just to be perfectly honest, I think that's really all you can ask for. But that's going to be the exception, not the rule.

MR. LOUTHAN: I would say that, of course, we don't need a SLC. I mean think about we're calling it the SLC. There's a reason for that, okay. This is what the customer pays. I don't know of any carrier that has the opportunity to charge the full SLC that chooses to only charge a dollar. They all charge the full 6.50 or 9.20. It's part of the local rate and it makes customers feel better because it makes it look like they're regulated rate looks 30 percent smaller than what it is if they were only paying for that line. But let's call it what it is. It's the local rate. Put it in the local rate and if you could rid of the local rate regulation and we look -- again, the CLECs don't have a SLC. Why? Like what the cable company charges. They charge about thirtyish dollars because that's what the market will bear and it just puts the telcos to a disadvantage.

MR. BERGMANN: We could go back to what the SLC was when it was first introduced, which, of course, was the interstate portion of the local loop.

But of course, that idea was abandoned a long time ago. So in the Missoula Plan and let's call it the Martin Plan for lack of a better term the SLC was just another revenue recovery mechanism. And I hope I'm remembering this right, but, for instance, in the Missoula Plan the idea was that in Washington, D.C., right here, the SLC would go up to $10, probably the lowest cost place in the whole country. But that interstate portion was supposed to go up to $10 as it would everywhere else.

And so I guess that's my answer to that question. If there are going to be increases in subscriber line charges, they need to be based on cost, not just across the board.

MR. ROSE: The SLC is in the federal jurisdiction, a federal charge and the local rates in the states -- and I agree with you, Frank, that it's essentially a local. The customer sees it as a local right, but they are in two different jurisdictions.

MR. QUINN: Victoria, I forget the second question.

MS. GOLDBERG: If the SLCs should pay a role in some sort of recovery mechanism, what should that look like? Should it be across the board? What about the concept of a variable SLC or some other kind of restructuring.

MR. LOUTHAN: Let the rates come up more to what is more of a market rate, and where there's competition those rates will not go up. And where there is not then maybe it needs to because the customers are not recovering the full cost. And we've made customers feel good by giving them a $14 bill and then we nickel and dime them in a bunch of other places to really recover the cost and eventually it's all collected, but the customer doesn't see that. Again, it's kind of the can of worms the industry has made for themselves over the last years, but ultimately rates are going to have to go up really on everybody, but there's going to be shock for a certain part of the market.

MR. MCKEE: It may be true that today most carriers charge the full SLC, not all do. And of course, you don't have to charge the whole SLC. The point is if you set the SLC too low then, yes, you automatically tack it on and it just becomes a part of the local rate. If you give enough flexibility in the SLC then you can allow the market to have more influence.

MS. GOODHEART: I want to ask if the carriers have any particular experience in an intrastate access reform and developing a recovery mechanism that maybe the FCC should look at, any lessons learned from state intrastate access reform?

MR. MASON: It's a tough question to answer because we've seen multiple states do various types of reform. We've had some that have gone and put state universal service funds in place. We've had some that have done longer transitions with very measured local rate increases and we've seen combinations of both. So it's hard to say which works best, but I think the principles that we talked about earlier, the same principles that we talk about in looking at intrastate access reform that everything be measured, that the transition be reasonable so that there's not a significant increase in any one step on the end user.

And part of that is obviously you don't want sticker shock on your customers, but I think as we talked about access line losses in our industry anything that's significant and creates shock also raises the risk that the revenue you're trying to replace you're ultimately going to lose through an increase in access line losses.

MR. QUINN: I think the lesson we learned is do it all at once fast because otherwise my son will be here in ten years talking about all this.

MR. MCKEE: I mean I guess the good news from the states is that you already have a lot of states that have already taken many of the steps, if not most of the steps that the Commission is proposing and disaster has not befallen them, so maybe that's just an encouragement that we can move a little faster.

MR. ROSE: I think a number of the states have a universal service fund that have accomplished some of this in the past. And I think it would be a good idea for the FCC to look at those to see how they work and not do anything that would upset what some of the states have already done because our members do depend on some of those state universal service fund for the low end of those access rates in the state.

MR. BERGMANN: I think there was an NRRI paper I think last year or the year before that evaluated the state universal service funds and some of those universal service funds were actually high-cost funds intended to make it easier for carriers to provide service in high-cost areas. Others of them, though, they're called universal service funds were actually revenue replacement funds and that's what is being currently being litigated in my state of Ohio. So I think we need to make a clear distinction between a state high-cost fund, which is what the federal high-cost fund is currently supposed to be and state revenue replacement funds, which is unfortunately what a lot of the funds actually are.

MS. TANNER: Rebekah, I'd be happy to share with you the Iowa process. We're struggling, so I don't know how informative it will be. But a couple of years ago the board did undertake some intrastate access reform and it was brought to us via the complaint process.

And in Iowa we have several rural carriers, upwards of 200 and together they serve about 225 calling areas. And these carriers joined together under the association tariff and the ITA, Iowa Telecommunications Association. The record showed in that proceeding that the average ITA member retail rates were unreasonably low while their switches access rates were unreasonably high.

To give you an idea of how low the local rates where, of these 225 calling areas 197 of those areas offered service below the national average of $15.03, $211 below Quest Iowa urban rates of $16.60 and 77 of those calling areas were below $10 a month.

On top of that, we found that the access rates charged were unreasonable. We had asked for support for the access rates. ITA responded that we mirror the NECA rates or that they mirrored the NECA rates. In truth, that was not the case. There had been some reforms, and I'll throw out the transport interconnection charge as an example, the TIC charge. Despite the fact that a lot of those costs had been reallocate to other rate elements, the ITA was still charging that.

Also, a lot of those services recovered under that charge, just tandem switching were performed by someone completely other than these ITA companies. They're performed by a group called INS. So what we found was that access rates were not cost-based. And we didn't have to have this discussion in Iowa should we do revenue replacement or cost replacement because by statute we have to move charges to cost and we also have to make decision that promote competition. So we needed to move those rates down to cost and we lowered those to the NECA rates, with one exception. By rule, we still charge a three cent CCL and we can't waiver on rules.

So all of this a really long way of saying we've started this process -- what we told your companies is if you still can't recover your cost bring a proceeding to the board. We have had a test case where a rural carrier said we can't recover our cost under the board's new rates and it has opened up a whole new set of issues for the board on what are costs because we were surprised to learn when they submitted these embedded separation cost studies that their version of cost is necessarily the cost of access. It's the cost again to run their company.

And I can't go into the details because a lot of them are confidential, but suffice it to say, in general, we found that there were costs or inputs in these separation studies that related to the non-regulated side of the company. Again, I don't want to get into confidential information, but things that didn't have a lot to do with providing interstate access or phone service, for that matter.

So all this is a long way of saying we don't have a state USF yet. We're looking at it, but we foresee the same problem in coming up with a state USF that we have in trying to set these access rates and that we don't have a good idea what the costs are to serve these rural area. Despite asking for information, we have not received it.

On the access cases, we tend to get data on the regulated piece and the only part we regulate is the intrastate access. But we don't know what the revenues are from the non-regulated pieces and we don't know what the costs are to serve.

And something else that came up when we looked at these inputs what troubled us on these separation studies is there does not seem to be any sort of prudency review on costs or expenditures. They're just automatically thrown into these studies. And so if I could turn my response to you Rebekah into a question for the panelists, I'd be really interested as we move forward in talking bout recovery, whether if it's federal USF or the Connect America Fund or state USF, who is reviewing the prudency of these costs? We're talking about ratepayer money. How do we know that these companies that the costs are necessary, that they're efficient? I know that some of our carriers in Iowa do ban together for efficiencies of scale, but I don't know to what extent.

And so I guess, in summary, our lesson from Iowa is that we still have no idea what it cost to serve these areas and this is after several contested cases. And going forward, as we're regulating less, and the broadband piece certainly states have less of a regulatory presence there, how do the regulators, whether it be a state or federal level know that these costs that carriers want to recover are prudent?

MR. MCKEE: That's an excellent point. I would love to be able to highlight and score that in transcript after you said it.

The reality is, from our perspective, none of these rates are related to cost. The actual incremental costs of providing these services is small, very low. And in fact, it's been going down steadily. And with IP technology, it's reducing even further.

So I agree with you 100 percent. There needs to be some kind of reality check and close scrutiny of what these costs are and whether or not there really is need or is this preserving a profit stream.

MR. QUINN: I think we have got to take a step up here because, respectfully, if the Iowa Commission doesn't understand the cost of the carriers in providing the access services, the FCC isn't going to be able to do that either. And just from a resource perspective, we're fighting a battle that to me is already lost. We've got to bring it up and focus on moving to a broadband fund where you're supporting broadband and trying to get it, not trying to determine what switched access costs are. I mean because the reality is in ten years -- I'll be amazed if in ten years there will be some portions of the PSTN still around in ten years, but there won't be many.

And if the FCC has really effectuated its National Broadband Plan goals, we're going to be dealing with a broadband environment that is going to be fundamentally different. And I think as you see next generation technologies come to fore in terms of providing broadband I think it's going to give you the opportunity to get out of the business of trying to determine at some minuet level of detail what the appropriate cost are.

Joel Lubin and I have been talking about - we used to talk about access cost all the time, right? But that day is so far behind us and if we stay mired in trying to figure out what happened ten years ago, we're never going to get to where we need to be in ten years. I respect the effort. We don't have local infrastructure in Iowa. We're a long distance provider there. I absolutely respect the effort, but the reality is, is the PSTN is going away and all of those issues are embedded in the PSTN. And if we haven't figured them out yet, we've got to create a proper infrastructure that supports broadband that's disciplined by efficient technologies. We've got to get out of the business of subsidizing competition and really trying to address the real issues of what the costs of providing broadband in rural American is going to be.

MR. LOUTHAN: Krista, you've got an inevitable position with the number of carriers you have in your state, but it is unusual. And if you back one stream out of that couple hundred thousand lines I mean they said not let the perfect be the enemy of the good. Unfortunately, it leaves in a worse position, but we're talking about these little, tiny LECs that maybe are putting one over people and are making massive profits. There are just not that many of them.

And in the grand scheme of what else we could do for the industry that could bring some more certainty and move forward there are probably some other policy decisions. And if a couple of guys gets through the cracks, then it is what it is. That doesn't change your directive. I understand. If you look at it, you're saying from the big picture there's a lot more out here that needs to be addressed.

MR. QUINN: Frank, I've got a question for you, which is how is putting the right framework in place going to -- I mean to me I look at Iowa and we've got 200 carriers in Iowa and I've got to say that at some level the word "consolidation" comes to mind. Do we really need 200 carriers in Iowa? But we've got create a framework I would think that's going to maybe do something to address that issue. Is creating an appropriate framework going to get us to an area where we have a more manageable number of carriers?

MR. LOUTHAN: From what I see with the smaller carriers, they're generally family-owned. This gets to a very emotional issue. It's a family-owned business, great grandfather founded the business. They don't want to give it up. It is what it is.

MR. QUINN: Yes.

MR. LOUTHAN: Now you make some changes that squeeze the business model and that'll force some of them to change. They'll have no choice. There definitely should be consolidation. There's no reason for there to be that many carriers. No reason for them to be that many carriers besides that. But when you have a family-owned business, it's just harder to force that kind of consolidation.

MR. GOODHEART: Is there any other

questions? We only have about ten minutes left.

MS. TANNER: Can I follow up real quick? I agree with you. I don't think we should spend a lot of time figuring out the proper intercarrier compensation rates. I think they're going down and that will be a moot point eventually. But my point is the lack of data. And there will likely be a recovery mechanism. It probably won't be intercarrier compensation, but it might be a state USF and there is a big problem at the state level -- I don't know about the federal level -- in getting the appropriate amount of data from the carriers to justify these costs. And how do we determine the appropriate recovery mechanism, if there is one, without any kind of data?

MR. LOUTHAN: If you put a low number out there, you might get some data.

MR. ROSE: There are about 140 companies in Iowa. And a good chunk of them, and I'm thinking maybe half of them are on what's called average schedules. And that is somewhat of an incentive mechanism and they don't do the separation cost studies and their return on access is based on formulas developed by NECA. So those guys probably don't have the data that you're looking for and they're not on a cost basis. They're on an average schedule basis and I'm not so sure whether it would be worthwhile to push all that to get a cost-based separate between state and interstate and all that. But I would think the majority of those 140 companies in Iowa are on average schedules and that's a different way of looking at things.

MS. KROENBERG: I really didn't have a question. I just wanted to make a point. And that is, when I heard Commissioner Tanner talk about the experience of obtaining the information to understand what it is that you're replacing to me it's a lesson for all of us to be learning. And that is, every day it seems while I'm here at the office someone is coming to me and saying that we're going to need money for broadband build out. And the lesson that you've now had how much money do they really need and is it really being prudently spent is an important one because we do have a limited fund. We have a commitment not to grow the fund and it's going to be a difficult task for all of us but I think one that we need to listen very closely, go back to the transcript that's highlighted and underlined that Charles is going to have of what you had to say because I think it's an important thing for all of us to be thinking about.

MS. GOODHEART: We only have about 10 minutes left. Peter, did you have a question you'd like to ask?

MR. MCGOWAN: Yes, I guess maybe just a small one that follows up a little bit on this point, but let me ask what maybe is a more threshold question, which is my sense is that some of you guys are doing what you are doing because you're competing. You're competing against other providers. And I know that competition is everywhere.

In Iowa, there apparently is enough competition to have the legislature relax end user rates. In New York, we have long understood that there's a lot of competitive pressures such that 90 plus percent of the state, including a lot of rural areas have at least three platforms. So I guess there is a lot competition out there and I know that this reform is going to be painful, but the question I guess I want to ask is should competitive carriers be allowed to get a contribution to supplement its cost recovery?

And with that question, I'm assuming that there is increased flexibility on your end user rates. So if you have increased flexibility on your end user rates and your access charges are being reformed, are you saying that you have a claim for recovery from USF?

MR. LOUTHAN: I don't see a business case for a competitive carrier to go into some place were the revenue is so low that it requires a subsidy unless the carrier sees that subsidy as making it massively more profitable than going somewhere else. So I would say there's an arbitrage that's going there just by definition. That would be my simple analysis, but I could be wrong.

MR. MCKEE: I mean from Sprint's perspective if you've got competition in an area, to your point, why are you doing subsidies at all? So if you've got multiple carriers and you have entrants who come in and built out plan and are providing services, and they're doing that without a subsidy then why do we need the subsidies in that area?

The issue becomes one of the ability of competition to then enter. So if you've got one player in the market who's receiving government subsidy and therefore have a built-in price advantage over all new competitors or all new entrants that's going to suppress competition in that market. So the question is how do deal with the issue of encourage new entrants.

You can either do it by saying no subsidy for anybody or everybody gets the same subsidy. Frankly, we're more than happy to say, yes, let's just eliminate the subsidy and let people compete.

MR. LOUTHAN: I would argue that would only be the case if the competition came into a hundred percent of the territory, and that's not what I see. I see a highly profitable area of a small town and a competitor comes and take that. But then you've got the family farmhouse down the road they don't bother to go to that one. So if the competition was going to a hundred percent, and you've got to remember that highly profitable center of town is subsidizing the vastly unprofitable other parts of the network and it gets imbalanced.

MR. MCKEE: And then the issue becomes how are you going to deal with subsidy for that area? So shouldn't your subsidy be directed towards that area and not directed towards that more profitable part of town?

MR. QUINN: But the subsidy is determined today based on the average cost that average out, both the competitive areas and the non-competitive areas and you have to target that -- I mean you could cut the subsidy out from the town, but that just means that the cost of servicing the farm may be even higher than what -- certainly higher maybe even perhaps than the average between the town and the farm, if the study area is large enough.

I mean there's not an easy solution to that problem. I think you have to deal with the doughnut and the doughnut hole, And you're going to have to determine in the town if you went and completely disaggregated in the town it may be that there is no need because there's a cable company there. There's a wireless company there. But then you'd have to determine what the cost of providing broadband to the farm is going to be because I guarantee you nobody is coming out to the farms.

MR. MCKEE: I've heard a lot of talk about the doughnut and the doughnut hole, but the reality is that in a lot of these areas that's not the population that we're really talking about. We're talking about areas that were at one time rural that are no longer rural, that are now suburban communities that are being treated as if they're still rural.

I mean the point is there has to be a realistic assessment of the need in a particular territory, and there may very well be doughnuts and doughnut holes in certain areas, but that doesn't mean there doesn't need to be some more critical analysis of those costs.

MR. ROSE: I think it was five or six years ago when Newbar did such a study about getting what they called the implicit subsidy and averaging over a large area. And the way I read that study that if you did that for that particular company that they would need more money to support that area that they were supporting by averaging.

I think the doughnut and the hole is a real issue. I think a lot of our companies some of them may be 50 percent, some of them 80 percent. We haven't really looked at it, but the doughnut and the hole is a real issue. If you disaggregate, and I think the FCC has looked at it, and rightfully so that they want to disaggregate before they address that doughnut and the hole issue. I think that's something that really should be done, disaggregate first, then you can have the data that you're looking for to make that decision.

MR. QUINN: I think the important thing to point out too is remember what we were doing here is were subsidizing to provide voice service. And I think it's very instructive if you look at the last competition report where I think that the share of

ILEC voice access lines -- it excludes wireless for reason that are beyond me, but it excused wireless, but the number or the percentages down below 70 percent. It's 69 and change in terms of the ILEC market share, if you will, for interconnected VoIP lines and wireline traditional TDM voice lines, which if you accept what I consider to be a conservative number that 25 percent of the market has gone wireless only that really translates into about a 55 percent market share.

And I think if you looked at the minutes, the actual voice minutes my guess is for the entire ILEC wireline industry when talk about voice as a service I would say their market share is probably in the 30s. I think that just underscores the problem that we have.

MS. GOODHEART: I think that this is a great conversation, but we only have five minutes and I'd like to get one last question in. And think John Baker will ask our last question.

MR. BAKER: Thank you. Near the start of our session Rebekah was asking you all about the transition period and I have a question about that, which is during a transition period how should we structure intercarrier compensation to encourage migration to enter the protocol transmission technology for call termination? That's one of our concerns about terminating carriers would want to shift to IP technology.

MR. MASON: Is the question more about how we deal with IP traffic as this morning was, but the transition to an IP network?

MR. BAKER: Yes, it's about design the program to give incentives to shift.

MR. MASON: I mean that's a good question and I don't know specifically what you do to incent engineers to move it, but I can tell you that it's starting to move in that direction already. Legacy switches are not supported by the vendors in the same way and so there is at least some evolution as switch capacity gets fully utilized. But we're out there unitizing soft switches in our network today. And we do identify that there are efficiencies in those as you go to routers and soft switches versus remotes and hosts, but it's not something that's going to happen overnight. It's a significant amount of investment. While ultimately you become more efficient, you still have a lot of replacement that you have to do in legacy network.

MR. BAKER: But the design of the program doesn't influence the speed of that transition?

MR. MASON: I don't know that the design of the program does or doesn't, right? I mean ultimately it changes the compensation under the current network, but I don't know that it incents a move.

MR. ROSE: Our guys are putting in a lot of soft switches replacing the old switches, and soft switches are far cheaper than the old switches are. So they're going to the soft switch. Soft switch enables the companies to send the stuff on an IP basis up the connecting carrier. There are times when the connecting carrier hasn't changed his end to an IP basis, but as more and more soft switches are deployed the capability to go an all IP world is there. And I'm not sure how we design or we structure a mechanism. I think if we get a good restructure mechanism I think it would be okay because our guys have got replace those old switches any way. And I think a new soft switch not only probably will be cheaper, but it allows you to send it to IP lines.

MR. MCKEE: I think the risk you have is the longer you make the transition the less incentive there is to reduce cost. And one of the ways of reducing costs is moving to an IP platform.

I mean there's a joke around our office that

Bob's comments really reminded me of, and that was last one on the PSTN writes a check for $8 billion. That last minute is going to be really expensive. So I think the fact is you can't avoid making this happen fast.

MR. BERGMAN: The last thing I would say is that if your process and results are going to be data driven, one of the things you need to look at is the theme that's in the notice of proposed rulemaking that high access charges have disincented the switch to a broadband network when, of course, it's exactly the smaller carriers that have the higher access charges that have done more broadband build out than the larger carriers.

So if you're going to look at the data, which we very much support the FCC doing, that's a key datum that you need to look at in terms of one of the fundamental premises behind this pressure to reduce intercarrier compensation.

MR. LOUTHAN: I would just caution the commission with the obsession with forcing carriers to go to IP because it's going to be cheaper. I'm not sure that notion needs to be rammed through as quickly as sometimes I -- at least it comes through in documents that I read. This is happening naturally anyway and there is not a small cost, necessarily, to going -- you have a TDM that's working perfectly well for certain parts of the rural LEC network. Just let it continue to work.

What will really change that and go to IP is when the business model changes. And I'll tell you when the business model is going to change is already on the way. It's called 700 MHZ with LTE built over it. So be careful what you wish for about not subsidizing your back call carriers as you've just agreed to build out 20 percent more LTE. At some point that's going to change the business model, then those carriers will be pushing fiber to towers. They'll be pushing fiber deeper in their networks and that's naturally going to transition to IP. And to try and make them go IP quickly there's a check they're going to have to write and this whole conversation is about companies that don't have enough revenue already. So I would just let that naturally happen.

MS. GOODHEART: I want to just clarify a point about, David, I think the NPRM talks about a disincentive to IP interconnection, not sort of the entire network. They were trying to promote goals to accelerate the transition. We recognize that the small carriers have been using USF and ICC to build out the last mile for their IP.

But anyway, it's a little over time, so I wanted to thank our panel today for coming. It was a very engaging discussion. We will have our second workshop, which will focus on Universal Service and the Connect America Fund, on April 27 here at the FCC. Thank you.

(Whereupon, at 3:03 p.m., the workshop in the above-entitled matter was concluded.)

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REPORTER'S CERTIFICATE

TITLE: Intercarrier Compensation Reform Workshop

DATE: April 6, 2011

LOCATION: Washington, D.C.

I hereby certify that the proceedings and evidence are contained fully and accurately on the tapes and notes reported by me at the hearing in the above case before the United States Federal Communications Commission.

Date: April 6, 2011

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